

# NEW SOURCES OF LOCAL REVENUE

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Report of a Study Group  
of  
The Royal Institute of  
Public Administration

GEORGE ALLEN AND UNWIN LTD

In recent years there has been a trend in local government finance which must alarm all those interested in a healthy and vigorous system of local government. Local authorities are deriving a progressively smaller proportion of their revenue from income whose amount they themselves determine and a correspondingly larger proportion from central government grants. The result can be seen in increased administrative control by the central government and a loss of local autonomy.

This book is the result of an investigation by a study group of the Royal Institute of Public Administration into other possible sources of revenue for local authorities. An analysis is first made of the present position of local government finance in Great Britain. The report then describes the methods of financing local government in other countries and includes an account of the local income tax levied in Sweden. It proceeds to examine a number of local taxes imposed elsewhere to see if they could be recommended for Great Britain, and concludes by making a series of authoritative recommendations for new sources of local revenue which will effectively reverse the trend towards increased dependence on central government grants.

*See back flap*

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# *New Sources of Local Revenue*

REPORT OF A STUDY GROUP OF  
THE ROYAL INSTITUTE  
OF PUBLIC ADMINISTRATION

PUBLISHED FOR  
THE ROYAL INSTITUTE OF PUBLIC ADMINISTRATION

LONDON  
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## LOCAL REVENUES IN ELEVEN OVERSEAS COUNTRIES

A duplicated supplement to this report contains information on the structure and finance of local government in the following countries:

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NEW ZEALAND

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SOUTH AFRICA

SWITZERLAND

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## PREFACE

THE Royal Institute of Public Administration has embarked on a series of major research projects on problems of outstanding importance in public administration. One of the first subjects chosen was an investigation into the possibility of finding new sources of local revenue for local authorities in addition to those already open to them; the present volume is the result of two years' intensive research and discussion by a study group appointed by the Institute.

This topic was chosen because of the Institute's growing concern with the trend of local government finance in Great Britain. Local authorities have come to receive a progressively smaller proportion of their income from revenues under their own control, such as rates, and a correspondingly larger proportion from central government grants. This trend is not in the best interests of a healthy and vigorous system of local government. Increased financial aid from the central government leads to greater administrative control from the centre, with the result that local autonomy is reduced and the responsibility of local authorities to their electorate diminished. It therefore appeared to the Institute that it would be an advantage if this trend could be halted and, if possible, reversed: with this aim in view it sought to find out whether there were other sources of revenue which might reasonably be granted to local authorities in addition to those they already have.

For this investigation the Institute set up a study group charged with the responsibility of carrying out a detailed enquiry and drawing up a report. This report constitutes the main part of this book. In the preparation of the report, the group have been mainly concerned with the problems of local authorities in England and Wales, but their recommendations will, it is thought, be of considerable interest to those concerned with local finance in Scotland and in Northern Ireland.

The names and descriptions of the members of the study group are listed on page 5. All the members of the group served in an individual capacity, and the organisations by whom they are employed, or with which they are connected, do not accept responsibility for the opinions expressed in the report. It will be seen, however, that the study group reflected the experience and the points of view of both central and local government, and included valuable representation from the universities. The Institute was indeed fortunate to secure the

services of men and women with such wide knowledge and experience, and the willingness to devote the time necessary to a research project of this magnitude. To all members of the study group the Institute wishes to record its sincere thanks.

It is particularly indebted to the Chairman, Mr. F. A. Cockfield, on whom the greatest burden of the work inevitably fell. He brought to the enquiry a profound knowledge of the British system of taxation, a clear understanding of the purpose of the study, and the leadership necessary for its accomplishment.

The Institute would also like to express its gratitude to Sir John Wrigley, who ably deputised for Mr. Cockfield on the occasions when he was unable to be present owing to absence abroad on business.

The study group was served by a full-time research worker and secretary, Mrs. E. B. Wistrich, and the group have expressed their high appreciation of her services. Mrs. Wistrich was largely responsible for the research into local government finance overseas, which formed the background of the enquiry, and she visited the Netherlands and Western Germany to undertake a special investigation into local entertainments taxes in those countries. Both in the preparation and study of material throughout the work, and in drafting the final report, she made a most valuable contribution. Her ability and hard work greatly facilitated the despatch with which the study group was able to complete its work.

The study was financed by a grant from the Nuffield Foundation, and the Institute wishes to acknowledge its indebtedness to the Trustees of the Foundation for their generosity, without which the enquiry could not have been undertaken.

In the course of this study monographs were prepared on the sources of local authority revenues in eleven other countries, namely Australia, Canada, Denmark, France, the Netherlands, New Zealand, Norway, South Africa, Switzerland, United States and Western Germany. The Institute is placing these monographs on sale as a duplicated supplement which will be available at the price of 10s.

Included in this book as a supplement to the main report is a full description of the system of local income tax in Sweden, prepared by Mr. A. L. Imrie, City Chamberlain of Edinburgh, and Mr. L. S. Murphy, late H.M. Senior Principal Inspector of Taxes, following a special visit of enquiry to Sweden. The Institute is greatly indebted to Mr. Imrie and Mr. Murphy for undertaking this important task, and to all the helpers in Sweden who are listed in the Foreword to their report. Mr. Murphy was also good enough to attend all the meetings of the study group where the subject of a local income tax was discussed.

## PREFACE

In connection with the enquiry into local entertainments taxes in the Netherlands and Western Germany, the Institute would like to acknowledge the help received by Mrs. Wistrich in the Netherlands from Mr. A. M. van der Ham (*Instituut voor Bestuurswetenschappen*), Mr. Braszcz (*Vereniging van Nederlandse Gemeenten*), Miss H. F. Maaldrink (*Ministerie van Binnenlandse Zaken*), Mr. W. Kleijn Molekamp (*Gemeente 's Gravenhage*), Mr. A. P. J. van Bastelaar (*Gemeente Wateringen*), Dr. Vulsma (*Nederlands Cultureel Contact*); and in Western Germany from Dr. Dr. Jansen (*Innenministerium, Land Nordrhein-Westfalen*), Dr. Lingemann (*Landeshauptstadt Düsseldorf*), Dr. Kottenberg (*Deutscher Städtebund*), and officials of *Wirtschaftsverband der Filmtheater*.

Much of the information contained in this report has been obtained through the valuable co-operation of government departments and local authorities in the United Kingdom and in the foreign countries to whose experience the group has referred. For this the Institute would like to record its warmest appreciation.

The Institute also wishes to thank other friends abroad who went to much trouble to answer enquiries on different aspects of local finance in their own countries, including Mr. H. Daalder (the Netherlands), Mr. R. Guibal (France), Dr. H. Seip, M.P. (Norway), Mr. Rangel-Nielsen (Denmark), Dr. L. P. Green (South Africa), the *Institut Finanzen und Steuern* and the *Deutscher Städtetag* (Western Germany), and the Municipal Finance Officers' Association (U.S.A.), Professor R. M. Clark (Canada), and the Canadian Tax Foundation.



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## Chapter I

### THE FIELD OF OUR ENQUIRY

OUR terms of reference invited us:

- (i) To survey the policies and practices followed in the United Kingdom and overseas for the purpose of providing revenue for local authorities;
- (ii) To report on the administrative practicability and probable effect of applying in the United Kingdom any of the policies and practices in operation elsewhere;
- (iii) To consider whether there can be devised any alternative sources of local revenue other than rates suitable for adoption in the United Kingdom;

and to report.

The assumptions underlying our report have been:

- (i) That it is accepted policy to look to local government for the performance of a wide range of functions. Both political parties have expressed their belief in the maintenance and development of local democratic government, with increased responsibilities.
- (ii) That it is accepted policy that local authorities should be recognised as responsible bodies, competent to discharge their own functions. The conception of the administrative freedom of local authorities is stressed in the First Report of the Local Government (Manpower) Committee which was accepted by the Government and approved in the statements issued by both political parties.
- (iii) That increased responsibilities, and administrative freedom in the exercise of them, must be accompanied by the ability of local authorities to finance their services largely out of resources at their own disposal, and that undue dependence upon the central government must be avoided if the general objectives of policy set out above are to be secured.



It is with the financial resources at the disposal of the local authorities that our study has been mainly concerned. But since the adequacy and suitability of these resources must be looked at in relation to the total burden of local government responsibilities, and to the nature and extent of their other sources of income, we thought it appropriate in the first place to consider briefly the extent of local government responsibilities, the current trends so far as we can judge in the distribution of responsibility for public services between central and local government, and the distribution of the cost of local government services between rates, government grants and other forms of income. Chapter II of our report summarises the results of this examination.

A striking feature of the last forty years or so has been the progressive increase in the dependence of local authorities on government grants, which supplied 22 per cent of total revenue in 1913-14, 35 per cent in 1938-39, and increased to 42 per cent in 1953-54. On the other hand, rate revenue has shrunk from 68 per cent in 1913-14 to 49 per cent in 1938-39 and 39 per cent in 1953-54. These are the figures for local authorities in England and Wales as a whole. In certain areas, dependence on grants has become much greater. In 1951-52, for example, 81 per cent of one county's income, and 73 per cent of one county borough's income, were derived from grants.

It appeared to us that a continuation of this trend was calculated to undermine the financial and administrative freedom which is recognised as a main objective of policy; and a main purpose of our study has been to examine possible methods of halting, and to some extent of reversing, this trend. We have also had in mind that because local authorities may levy only one tax, their discretion to decide how they should raise revenue to meet their expenditure is confined within very narrow limits.

Our next step was to consider whether this objective could be secured by an expansion of the one source of revenue which is at the sole disposal of the local authorities, i.e., the rates. In Chapter III we have examined the rates as an instrument of taxation, and, as will be seen, have concluded that, while the rates are a valuable source of income and should in our view remain as the main basis of local government revenue, and are indeed capable of some expansion, they are not suitable or adequate as the sole basis of such income. We believe also that however good a tax may be, continual increases in the charge accentuate its anomalies and give rise to criticism probably out of all relation to the amount of additional revenue involved. Many examples of this can be found in the field of national taxation and we believe that much of the criticism of the rates stems from this source.

We have therefore examined other possible sources. We have not regarded the word "alternative" in our terms of reference as having any very special implications. Any new source of revenue or income must be an "alternative" to some existing income, in the sense that it either replaces it *pro tanto*, or avoids the necessity of raising or obtaining additional money from the existing sources. But we desire to make it clear that we have not been thinking in terms of alternative sources of income which would entirely replace the rates. It would, in our view, be neither practicable nor desirable to do this. Our examination of what appeared to us to be possible alternative sources of income is made in Chapters VII to X, and in Chapter XII we have made our recommendations for what appears to us to be the most appropriate priority.

Selection will depend both on the suitability of the tax as a local government tax, and on the amount of revenue which it is likely to yield. The amount of revenue required is that which is likely to put, and to keep, local government finance on what we conceive to be the right footing, namely that the revenue from the taxes at the disposal of the local authority should not be less, and should preferably be more, than the amount of grants paid by the government. The amount required for this purpose will depend on the future scale of responsibilities of local authorities, and on the flexibility of the income derived from rates, which, in itself, may be substantially influenced by decisions on rating. Recognising these uncertainties, we would nevertheless say that, in our minds, in order to attain the objectives of policy which we have postulated, we have regarded an additional income of not less than £100 millions (over and above any additional revenue which might accrue from the rates) as a suitable objective to seek.

We know that the imposition of any new tax must be unpopular. It will, moreover, be represented as an attempt to increase the total burden of taxation and attacked on this ground. But we do not regard this as the right way of looking at the matter. Given the level of local government expenditure, the money must come from somewhere, and if it does not come from taxes levied by local authorities it must ultimately come from taxes levied by the central government. Unless the rates are to be driven up continuously, the choice really is between widening the taxing powers of local authorities and thus giving them direct control over their own revenue, or leaving it to the central government to raise the revenue required through its own taxes and to distribute the proceeds to local authorities by way of grants.

We realise also that many of the proposals we make may be criticised on a number of grounds. It is possible to draw up a formidable



indictment of any tax. In the ultimate analysis, however, if local authorities are to raise a bigger proportion of their own revenue through taxation, they can only do so by increasing the rates or by imposing other taxes. The real issue is whether the alternative taxes would not be better than further substantial increases in the rates. Thus it is a mistaken argument to contend that a local income tax would be indefensible because it made no distinction for differences in family circumstances, for the rates not only ignore family circumstances but they are regressive as well. We have reaffirmed our belief in the value of the rates as the main source of local government revenue, but we think it should be clearly recognised what in fact are the virtues of the rates. They are:

- (i) The rates are an old tax and are widely accepted;
- (ii) They are easily and economically administered and collected;
- (iii) They provide a stable source of revenue.

Their defects are too well known to need repetition. It is important, we feel, that in considering possible alternative sources of revenue, natural reluctance to make any change does not lead us to regard the rates as endowed with more virtue than they possess, or to criticise alternative proposals on grounds which in fact are equally applicable to the rates.

We would say finally that in no way do we subscribe to the opinion that local government finance has broken down. What we do say is that for a number of years the trends in the source of their finance have been in the wrong direction; and that the time has come to halt these trends, and to seek new sources of revenue which will reduce, rather than increase, the dependence of local government upon government grants and give back a greater measure of financial independence to local authorities.

In many respects the situation in which local government now finds itself is very similar to that which faced the central government towards the end of the eighteenth century. The national revenues were then derived almost wholly from indirect taxes. No one would contend that indirect taxes could be dispensed with, and indeed they still account for about half of the total tax revenue. But it is equally clear that had the new direct taxes on income and capital not been brought into play, the modern state as we know it to-day could never have developed. In our view, local government now finds itself in much the same position. Unless in the comparatively near future its revenue base can be extended, the development of local government itself must be confined and frustrated.

## Chapter II

### SOURCES OF LOCAL REVENUE IN ENGLAND AND WALES

THE extent of the present responsibilities of local authorities is the result of a long process of growth and adjustment. During the latter part of last century and the earlier part of this century, the growth of local government responsibilities was continuous. It was commonly stated after the passing of the Local Government Act, 1929, that the range of services of local authorities covered the citizen from the cradle to the grave—maternity and child welfare, education, housing, hospitals, poor law relief, cemeteries. During more recent years the range of functions of local government has been reduced, as a result of the assumption of greater responsibilities by the central government, particularly for financial assistance for those in need and for the provision of hospitals and of medical services. In addition, local authorities have lost most of their trading services as a result of the nationalisation of gas and electricity. On the other hand, there has been a more intensive development by local authorities of those services for which they have retained responsibility, e.g., education, housing, welfare and the protection of children.

The changes in the rate fund services are illustrated by the figures of the expenditure of local authorities on revenue account for these services:

<i>Year ending 31st March</i>	<i>Expenditure on Revenue Account</i>
	£m
1891	39
1921	246
1931	321
1938	372
1954	978

Even allowing for the rise in prices which occurred as a result of the First World War, it is apparent that during the period up to 1938 the

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expenditure of local authorities showed an absolute increase; between 1938 and 1954, having regard to the rise in prices which took place, the rise in local government expenditure has been approximately only equivalent to the increase in the price level.

This general impression needs to be corrected by some illustrative examples of the changes in the amount of the expenditure on a few major services which, between them, have at different times constituted a large part of the expenditure of local authorities.

Names of Services	Year ended 31st March,	
	1938	1954
	£m	£m
Poor law, personal health and welfare .. ..	57	81 <sup>1</sup>
Education .. ..	84	364
Housing .. ..	34	140
Highways .. ..	44	78

The most striking feature of these figures is the absolute and the comparative increase in the part which education plays in local government expenditure. Education, housing and highways have always been accepted as services suitable for local administration, and both the main political parties have expressed themselves in favour of giving a greater share to local government in the administration of the Health Service. We therefore feel justified in assuming, from the trend of events over a long period, that the range and scale of services for which public responsibility is accepted are not likely to decrease, and we see no reason to expect from the pronouncements of political parties that the part to be played by local government in the discharge of these responsibilities will decrease.

We turn next to the trend of events in regard to the financing of local government services. In the published *Local Government Financial Statistics*, services are divided into:

- (a) Rate fund services;
- (b) Trading services and corporation estates.

The distinction between them is not a precise one; it is a matter

<sup>1</sup> This figure includes local government expenditure on the care of the aged, handicapped and homeless, the protection of children and individual health.



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rather of convention and convenience than of a clearly defined distinction between services which are self-supporting and services which involve a charge on the rates. It is the task of meeting the expenditure required for the rate fund services which constitutes the basic problem of local government finance. With reference to services and their financing, we have, therefore, confined our attention to rate fund services. Revenue for rate fund services is derived from three sources, which are classified in the *Local Government Financial Statistics*:

- (i) Fees, rents, recoupments, etc.;
- (ii) Government grants;
- (iii) Rates.

The distribution of expenditure between these three sources is indicated by the following figures:

Year ended 31st March	Expenditure on Revenue Account		Income from fees, rents, recoupments, etc.		Government grants		Net expenditure met from rates and balances	
	£m	%	£m	%	£m	%	£m	%
1931	321	100	49	15	128	40	144	45
1938	372	100	58	16	135	36	179	48
1954	978	100	186	19	414	42	378	39

The proportion of the total expenditure on rate fund services which is met by fees, rents, recoupments, etc., has steadily increased from 10 per cent in 1913-14 to 16 per cent in 1937-38 and 19 per cent in 1953-54. The income from this source is mainly derived from charges for services and, in particular, from the rents charged for municipal houses. The increased part which this source of income has come to play in the general picture of local government finance is primarily due to the continuous expansion of municipal housing since 1919.

We have already referred briefly to the question of government grants in Chapter I. The growth of the dependence of local authorities upon these grants plays, however, so important a part in our study, that we thought it appropriate at this stage to include some further analysis of the stages by which the present position has been reached.

It has long been national policy to look to local government for the discharge of a wide range of functions. These functions have, however, never been looked upon as a separate province in which

central government was to take no part and over which it was to exercise no control. Although the responsibility for initiating and carrying out the various services rests by statute with the local authorities, all the statutes dealing with the more important services are freely sprinkled with provisions which show that in effect the approval of some department of the central government is necessary for the exercise of many of the functions. The general requirement that all applications for loans must be approved and the district audit of accounts are other powerful weapons of control. Local direction is often further controlled by Government departments as a result of decisions taken by the Government on grounds of national policy as to the scale of capital expenditure and the purpose to which it should be directed, e.g., the changes in the years since 1945 as to the number of new houses which it was the objective of Government policy to secure.

Where particular services are grant-aided, further controls may become applicable, and these will vary either because of the nature of the grant or the extent to which the central government considers it necessary to fetter the discretion of the local authorities on grounds of national policy, or no doubt sometimes because of the cast of mind of the administration.

The grants which are payable in respect of specific services have taken a number of different forms determined by the legislation under which they become payable. The conventional classification of grants is on the following lines:

- (a) Grants payable on a percentage basis, usually based on net approved expenditure. These constitute the largest number of specific grants and are illustrated by:
  - (i) Class I roads—75 per cent.  
Class II roads—60 per cent.
  - (ii) Individual health, police and protection of children—50 per cent.
  - (iii) Fire service—25 per cent.
- (b) Grants based on a percentage, but a percentage which is variable between local authorities at the discretion of the responsible Minister on the facts of individual cases, or where the amount of the basic percentage is varied by the introduction of additional factors into the calculations. The grant for education is the chief example of a percentage grant which is variable by the introduction into the calculation of factors additional to cost. It takes the form of a main grant of £6 per unit of the average

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number of pupils on the register, plus 60 per cent of the net recognisable expenditure of the authority, minus the product of a 1s. 6d. rate in the area. (Prior to revaluation, this was a 2s. 6d. rate.)

- (c) Grants on a unit basis. The grant for new municipal houses which are being built at present is calculated in this way. The total housing grants now being paid each year also include, however, payments for houses built between the wars under various statutory conditions, for some, but not all, of which the government grant also takes the form of a payment per house.
- (d) Grants in which no amount or percentage is fixed by the authorising legislation, and in which the amount of the grant is left to be determined by the responsible Minister on the facts of the case. Examples of such grants are the grants for rural water supply and sewerage, land drainage, river conservancy, and coast protection.

While the published *Local Government Financial Statistics* do not distinguish between the grants paid in respect of different parts of the same service, it is clear that so far as the amount of expenditure under these varying forms of grants is concerned, the amount of the main education grant is much the largest factor, the percentage grants and the housing grants are substantial, and the expenditure under the discretionary grants is unimportant.

The form and amount of the grants paid for specific services result from a series of decisions taken over a long period of years in relation to these services individually. There does not appear to be any evidence that either the central government or Parliament has favoured one particular form of grant for specific services, either generally or at particular times.

Apart from the grants intended to promote the development of specific services which were accepted as objectives of national policy, it has long been accepted policy that a measure of financial assistance should be given by the central government towards the general cost of local government. The General Exchequer Contribution, under the Local Government Act, 1929, and the Exchequer Equalisation Grant under the Local Government Act, 1948, which subsequently took its place, were not paid in respect of specific services. The Equalisation Grant is based on the distribution of a sum of £61 millions in 1953-54 to those local authorities whose average rateable value per head of the weighted population was below the average.



The two main trends in regard to the payment of grants in recent years have been:

- (i) An increase in the total amount of grant-aid in proportion to the burden falling on the ratepayer. For every £100 falling on the ratepayer, government grants amounted to £89 in 1931, £76 in 1938, and £112 in 1954. During these years, financial responsibility was also taken by the central government for services formerly discharged by local authorities as poor law and public health authorities almost entirely without Exchequer assistance.
- (ii) An increase in the proportion of specific grants to unallocated grants. In 1931, 64 per cent of the grants were paid in the form of specific grants and 36 per cent in the form of unallocated grants. In 1953-54 specific grants had increased to 85 per cent and unallocated grants had decreased to 15 per cent. The total amount of specific grants has shown a continuous increase for several reasons. The central government has increased a number of its grants on a number of the more important grant-aided services, and there has been a great expansion in the scale on which they are operated. The upward movement of the price level has resulted in a great increase in the cost of the services and consequently in the amount of the grants paid on them. None of these factors has affected the general grants, which have in effect remained stationary in amount. The biggest single factor contributing to these trends is the growth in expenditure on education.

The decision as to the kind of grant to be made by the government must clearly be a matter of policy, as also must the decision as to the amount of the grant to be made in respect of a specific service, in so far as the decision as to this amount is determined by the degree of national, as distinct from local, interest, or by the desire of the government to exercise a greater measure of control over the operation of the service. It has, however, already been accepted as a matter of general policy in regard to local government services that local authorities should be recognised as responsible bodies competent to discharge their own functions, and that departmental control should be concentrated at key points, leaving the management of services as far as possible to the local authorities.

We are bound to assume, therefore, that the increased financial dependence of local authorities upon the central government has been due, not to a desire on the part of the central government to increase

its control over the administration of local government services, but to a feeling shared by the government and the local authorities that the financial resources at the free disposal of the local authorities were insufficient to bear without undue hardship their former quota of the expenditure under the existing rating system.

Local authorities can levy only such taxes as they are authorised by Parliament to levy. In fact, the only tax which Parliament has given them power to levy for the general financial needs of the district, is the tax on the occupation of land and buildings which is known as "rating." Local authorities have the power to levy whatever rates are necessary to meet their liabilities. In the next chapter we therefore examine the rating system and the part which it has played, and may be expected to play, in local government finance.



## Chapter III

### THE RATING SYSTEM IN ENGLAND AND WALES

WE now turn to the rating system and the reasons why rate revenues have not grown in proportion to local government expenditure. We have deliberately confined our survey of the rating system to England and Wales.

The system of rating has developed along with the growth of local government services and we shall at the outset describe its development and present structure. There are five basic points to be considered: the authorities responsible for levying and collecting rates, the people responsible for paying them, the properties upon which they are payable, the basis of the valuation upon which liability is based, and the authorities responsible for making the valuation.

#### THE AUTHORITIES RESPONSIBLE FOR LEVYING RATES

In the early stages of development, power to levy rates was conferred on the authority responsible for the service which the rate was to finance. The Elizabethan Poor Rate, the first statutory obligation to finance poor relief by a rate, was levied by the parishes. During the nineteenth century, many new local government services developed and were carried out by *ad hoc* authorities, with the result that the number of local authorities levying rates increased. The Act of 1888 established the county boroughs and the administrative counties, and the Act of 1894 transformed the urban and rural sanitary authorities into urban and rural districts. These bodies were all-purpose or many-purpose authorities and they gradually took over many of the functions hitherto performed by *ad hoc* authorities. The chief rates were now the poor rate, which included a number of other rates and was levied by the parish overseers, and the general district rates levied by the town and urban district councils. It was not until the Rating and Valuation Act of 1925 that the separate rates previously levied for different purposes were consolidated in one general rate to be levied throughout the area of the rating authority. Borough and district councils were made rating authorities, responsible for making and collecting the rates. They still retain these responsibilities and the county councils precept on the borough and district councils in their

## THE RATING SYSTEM IN ENGLAND AND WALES

areas for rate revenues. In addition to the consolidated general rate, there are the special rates levied in rural districts on particular parishes. Each rating authority levies its rate as a fixed sum for every pound of rateable value of each hereditament, the level of the rate being determined by the amount the authority needs to meet its own expenditure (and precepts from other authorities) after all other possible receipts have been taken into account.

### THE PEOPLE WHO PAY RATES

The earliest rates in England were levied on those inhabitants of a community who would benefit by the particular service which the rates were to finance. The Elizabethan Poor Rate is a landmark for it was levied on all inhabitants of the parish and all occupiers of land, houses and other property in order to finance poor relief, irrespective of the benefit individual ratepayers derived. Liability for the payment of rates was thus greatly extended and the burden of financing poor relief was spread over the whole of the local community. Occupiers of property were included to ensure that those who occupied property but did not live in the area made their contribution. The extent to which each inhabitant contributed rested on his ability to pay.<sup>1</sup> In assessing liability for taxation, the most important practical measure was a man's tangible property, particularly his house and land. In time, this replaced the general criterion of "ability to pay," and the rate became a tax, not on each inhabitant, but solely on the occupiers of property. The principle of taxing all occupiers of rateable property to finance local services remains an essential part of the present rating system.

### THE PROPERTIES UPON WHICH RATES ARE PAYABLE

As the basis of the rate was progressively narrowed, all forms of property other than land and buildings came to be excluded from the assessment. Under the present rating system, it is the ratepayer's visible estate in each rating authority area which is taken as the measure of his ability to contribute towards the cost of the local services in that area, and rating is thus applicable to all land, houses and other buildings beneficially occupied except insofar as they have been specifically excluded from its scope.

Property occupied by the Crown is not directly rateable at all, but compensating payments are made to the local authorities broadly equivalent to the amount which would be paid if the property were rated. Since the nationalisation of the railways and canals and of the

<sup>1</sup> "In modern phrase, the poor rate was intended to be a local income tax upon the inhabitants of the parishes." See E. Cannan, *A History of Local Rates*.

electricity industry, hereditaments occupied by them have also been taken out of the normal rating system. These nationalised industries make payments in lieu of rates, representing the revenue collected by the local authorities before nationalisation after certain allowances have been made, firstly for changes in the average rates levied, and secondly for changed circumstances within the industries; the amount thus calculated is then apportioned among the local authorities by the Minister of Housing and Local Government according to the proportion the rateable value of each area bears to the total rateable value of England and Wales. The 1955 Rating and Valuation Act provides a new method for the valuation by the Ministry of Fuel and Power of property belonging to the Gas Boards which allows for changes in the amount of gas supplied in each Board's area in calculating the rateable value; the rateable value for each Board is then apportioned among the rating authorities according to the ratio of the gas supplied in the rating authority's area to the gas supplied in the whole of the Board's area.

More important in relation to local authority revenues are the classes of property partly or wholly relieved from rating. A series of Acts between 1896 and 1929 have relieved a substantial number of hereditaments from rating. Although partial relief had previously been granted to agricultural land in respect of certain rates, the first general measure of derating was made in 1896, when agricultural land was derated by 50 per cent. In 1923 it was derated by a further 25 per cent and has been wholly exempted from rates since 1929. Agricultural buildings were derated by 75 per cent in 1925 and wholly derated in 1929 with agricultural land. Industrial hereditaments since 1929 pay rates on only 25 per cent of their net annual value. The decision to derate was taken primarily as a matter of national policy on the ground of the difficult economic conditions then prevailing, but in the case of agricultural land, there was a long history in the nineteenth century of pressure brought to bear in the interest of farmers and landowners for some relief from local taxation. By other statutory provisions, the premises of voluntary schools, churches, and scientific and literary societies are entirely exempted from rates, and the Rating and Valuation Act of 1955 has added to this list church and chapel halls and other premises used for religious purposes; it has given rating authorities power to remit or reduce rates on premises used for charitable, educational or philanthropic purposes, and on playing fields occupied by non-profit making societies and almshouses held on trust. All other hereditaments, including dwelling houses and commercial premises such as shops, offices and warehouses, are charged on their full rateable value.



## THE BASIS OF VALUATION

Since the rate developed into a charge on the occupier of property, it was early found that rental value was a convenient measure of rateable value. But as the poor rate was originally intended to reflect ability to pay, "just" rather than actual current rents were often used in making the assessments. It was the Rating and Valuation Act of 1925 which established more firmly the principle that valuation should be based on "the rent at which the hereditament might reasonably be expected to let from year to year." In the case of most industrial properties and the public utilities, the valuation assumed that the tenant paid rates and taxes and undertook to bear the cost of repairs. The value thus reached was the net annual value or rateable value. But the Act provided that for other premises, chiefly dwelling houses, the valuation was to be a gross value, which assumed that the landlord undertook to bear the cost of repairs, and deductions for such costs were then to be made on the basis of a scale prescribed by statute in order to ascertain the net or rateable value. The reason for the difference was that evidence in the case of industrial properties was mostly of lettings where the tenant carried out repairs, whereas for dwelling houses the landlord generally carried out repairs.

Under the 1925 Act, revaluations were to take place at regular five-year intervals. In fact, only two such revaluations were carried out, the last in 1934. When, for the third revaluation, it became known that the Central Valuation Committee (set up with advisory powers under the 1925 Act) had recommended strict adherence to the valuation provisions of the 1925 Act, there was so much apprehension of undue hardship to the occupiers of small new houses that the valuation was postponed pending an enquiry into the probable extent of hardship. Before any steps could be taken, the war had broken out. In 1945, therefore, rateable values rested on the revaluation of 1934, but that itself was still influenced by the rent controls of the First World War which were only gradually relaxed, and from 1939 rent control was once more imposed on nearly all dwelling houses. The Act of 1939 brought within rent control the 2-3 million new houses built by private builders in the inter-war period which had never previously been subject to rent control.

The first post-war attempt to lay down a new basis for a revaluation was contained in the Local Government Act of 1948. It provided for the revaluation of industrial and commercial premises on the basis of current rental values, but introduced a new method of valuing certain dwelling houses. Houses built before 1919 and the larger ones built after that date were to be valued by reference to the actual rents



charged for comparable houses in 1939. Small houses built after 1919 were to be valued at 5 per cent of the hypothetical cost of construction in 1938 plus 5 per cent of the 1938 value of the site. After a pilot survey had revealed substantial difficulties, this system was withdrawn by the Valuation for Rating Act, 1953. The 1953 Act, on which the present revaluation is founded, bases the assessment of all dwelling houses on "the rent at which the hereditament in question might reasonably have been expected on or about the 30th June, 1939, to be let from year to year." In arriving at the assessment, the valuer was to assume that the hereditament and the locality were in the same condition as they were at the time of the revaluation. The valuation of industrial and commercial hereditaments, as in the 1948 Act, is based on current rental values. The 1953 Act is thus an attempt to return to the rental basis. While on the whole there is good evidence of actual rents in 1939, in some cases there are implied complicated and speculative calculations for valuers. They have to reckon, for example, what rent a house built in 1955 would have fetched in 1939, as well as the effect on that rent of any change in local amenities and the state of the property itself in 1955 on that rent, before they can arrive at a gross value. It has, however, been expressly stated that the intention is to advance the basis date towards the present as circumstances permit.

#### THE AUTHORITIES RESPONSIBLE FOR MAKING THE VALUATION

The Act of 1925 transferred the responsibility for making valuations from the overseers of parishes to borough and district councils. It also set up machinery for appeals, County Valuation Committees, and a Central Valuation Committee with advisory powers. In spite of these efforts to promote a greater degree of uniformity in valuation, the number of independent valuation authorities was still so large that a continuing lack of uniformity was to be expected for this reason alone. That considerable variation in valuation practice persisted was recognised by the Committee appointed by the Minister of Housing and Local Government to investigate the operation of the Exchequer Equalisation Grant, which observed in its Report of 1953 that: "There are serious and widespread inequalities in the basis of assessment of various kinds of properties in the several local government areas of the country." These inequalities became the object of serious concern when the Exchequer Equalisation Grant was introduced in 1948. Since the equalisation grant is paid to all local authorities whose rateable value per head of weighted population is below the national average, uniformity in the making of the valuations which determine eligibility for grant is essential to its equitable distribution. In the same Act of

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1948 which introduced the Exchequer Equalisation Grant, Parliament provided that the responsibility for the preparation and amendment of valuation lists should be transferred from the rating authorities to the valuation officers of the Inland Revenue Department.

### DISTRIBUTION OF RATE LIABILITY ACCORDING TO THE TYPE OF HEREDITAMENT

The main burden of rates falls on the householder and the shop-keeper or office occupier, as the following analysis of rateable value for all local authorities in England and Wales on 1st April, 1956, shows:

Type of Hereditament	All Local Authorities		Administrative Counties (ex. London)		London		County Boroughs	
	£m	%	£m	%	£m	%	£m	%
Domestic ..	307.8	49.4	191.7	57.9	30.6	29.2	85.6	45.8
Shops .. ..	89.0	14.3	38.5	11.6	17.3	16.5	33.2	17.7
Miscellaneous <sup>1</sup>	170.1	27.3	68.3	20.6	48.6	46.4	53.1	28.4
Industrial ..	39.1	6.3	23.2	7.0	3.9	3.7	12.0	6.4
Freight transport	1.5	0.2	0.3	0.1	0.7	0.6	0.5	0.3
Crown .. ..	15.5	2.5	9.1	2.8	3.8	3.6	2.6	1.4
Total .. ..	623.0	100	331.1	100	104.9	100	187.0	100

Source: *Distribution of Rateable Values between Different Classes of Property in England and Wales*. Cmd. 9718.

The rateable values given above are the first since the revaluation. It is interesting to compare them with the pre-revaluation values, and to note the proportionate increases in rateable value for each type of hereditament. These figures, which refer to all local authorities in England and Wales, are provisional and subject to revision following individual appeals.

<sup>1</sup> Comprising commercial properties (other than shops), hotels, licensed premises, schools, etc.

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Type of Hereditament	Rateable Value		Increase in Rateable Value	Percentage of R.V. to Total		Percentage Increase in R.V.
	New Lists	Old Lists		New Lists	Old Lists	
	£m	£m	£m	%	%	%
Domestic ..	307.8	219.2	88.6	49.4	59.8	41
Shops .. ..	89.0	39.4	49.6	14.3	10.7	128
Miscellaneous ..	170.1	77.2	92.9	27.3	21.1	121
Industrial <sup>1</sup> ..	39.1	15.4	23.7	6.3	4.2	160
Freight transport <sup>1</sup>	1.5	0.7	0.8	0.2	0.2	114
Crown <sup>2</sup> .. ..	15.5	14.7	0.8	2.5	4.0	5
Total .. ..	623.0	366.6	256.4	100	100	72

The revaluation has thus resulted in an overall increase in assessments of 72 per cent. The assessment of shops has increased by 128 per cent, and of industrial hereditaments by 160 per cent, but domestic hereditaments have shown an increase of only 41 per cent. The result has been a change in the share of total rateable value represented by each class of hereditament. Domestic hereditaments have decreased in proportion to the whole from 60 per cent to 49 per cent, a fall of 17 per cent, while all other types of hereditament have increased their proportion of the whole by 33 per cent (shops), 50 per cent (industrial properties), and 30 per cent (miscellaneous properties including offices).

Revaluation makes no difference to the total amount of money required by local authorities to meet their expenditure, but it will affect the distribution of this expenditure between ratepayers. Because the Equalisation Grant is linked with rateable values, revaluation will also affect the amounts which will need to be raised from rates by different local authorities.

## RATES AS AN ELEMENT IN COSTS

An estimate of the relationship of rates to costs may be made by

<sup>1</sup> The rateable value of industrial and freight transport hereditaments used for industrial or transport purposes represents only 25 per cent of their net annual value.

<sup>2</sup> Crown property has not yet been revalued.



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reference to the figures of National Income and Expenditure. In relation to Gross National Product in 1955 (at market prices) rates paid on industrial and commercial hereditaments comprised only 1 per cent of the total. Rate payments by manufacturing industry represented only one third of one per cent of industrial output. The position will be affected by the revaluation of properties in England and Wales, but having regard to the increasing trend of the national output, any dramatic change in the relationship of rates to costs is unlikely.

### RATES AND HOUSEHOLD INCOME

One half of the total rateable value of the country is composed of domestic hereditaments. We have therefore given special consideration to the incidence of rates on householders. Incidence may be measured according to different levels of income; the family circumstances of householders at the same level of income; and the region or local authority area in which the householders live.

The income incidence of rates on families in Great Britain was analysed in 1938 by Professor and Mrs. Hicks. Data for 1937 enabled expenditure on rates as a percentage of total family expenditure to be calculated separately for the lower income groups in different parts of the country. Family expenditure was taken as approximately equal to family income after payment of direct taxes. Savings were excluded. The following average figures emerged for different groups; the figure for higher incomes, which is less well founded, is added for comparison.

<i>Income Per Annum</i>	<i>Total Net Income</i>	<i>Percentage of Total Incomes</i>	<i>Percentage of Income Paid in Rates</i>	<i>Total Rate Payments</i>	<i>Percentage of Total Rate Pay- ments</i>
	£m			£m	
Up to £250 ..	2,676	65	3.8	101	74
£250— ..	578	14	3.4	19	14
£500— ..	311	8	3.0	9	7
£1,000— ..	224	5	2.0	4.5	3
Over £2,000	340	8	1.0	3.5	2
Total .. ..	4,129	100	3.3	137	100

Source: National Institute of Economic and Social Research, *The Incidence of Local Rates in Great Britain*, J. R. Hicks and U. K. Hicks, 1945.



The average proportion of family expenditure paid in rates was thus found to be 3.3 per cent; the proportion was highest for the income group earning up to £250 per annum (3.8 per cent), and diminished as income increased.

A similar conclusion emerged from an examination of a comparison between the proportion which each income group contributed to the total of rates paid and the proportion of total income after tax which each group received. The comparison showed that in 1938, income groups of up to £500 per annum, receiving 79 per cent of total income after tax, paid 88 per cent of all rates, while income groups of over £500 per annum, receiving 21 per cent of total income, contributed 12 per cent of rates. The broad conclusion of the report was that, on the basis of conditions in 1938, rates on dwelling houses, which were essentially a tax on the occupation of house room, bore more heavily on ratepayers with low incomes than on those with high incomes, but that the variation in incidence was comparatively small for the great majority of families and that it was only over £1,000 per annum that the burden became very much lighter.

No comparable study has been made of the incidence of rates since then. We know that the burden of rates on income fell steadily during the war, to an average of roughly 2.3 per cent in 1944 (on the same basis); this was due to the great rise in money incomes and to the relative steadiness of rate poundages. It was only after 1945 that rate poundages began to rise steeply, giving rise to a widespread impression that the burden of rates had greatly increased. Although rate poundages are higher, the basis on which they are levied, rateable value, had shown a very small increase up to the revaluation; meanwhile money incomes have increased rapidly and the general level of prices has more than doubled. The amount of rates collected per head of the population in 1955/56 in England and Wales was in fact £8 19s. od. compared with £4 12s. od. in 1938/39, an increase which has not even caught up with the rise in prices and money incomes. Since revaluation, rateable values have risen and rate poundages have been lowered. But, from the ratepayer's point of view, the important factor is the amount of rates he has to pay, and this may not have greatly changed. Rates are therefore considerably less burdensome than they were in 1938 for the community as a whole.

It is, however, likely that there have been changes in the relative burdens borne by different income groups. Very considerable changes have occurred in the distribution of net income since 1939, largely the effect of steep progression in income tax and surtax. As a consequence, the incidence of rates in relation to net incomes from which they are

paid, may well have changed considerably. On the other hand, the post-war building drive has been mainly concentrated on the building of municipal houses. These new houses are assessed at higher figures than the great majority of the older rent-restricted houses, and the incidence of rates for householders living in municipal housing estates is therefore likely to be relatively high. This trend must be weighed against the effect of the redistribution of net incomes mentioned above. A recent analysis<sup>1</sup> of the incidence of rates based on a sample survey made in 1951/52 relates rates to gross income and shows on that basis that rates are regressive at the present time. The degree of regressiveness of rates in relation to *net* income (after direct taxation) may have been reduced to some extent, but it is improbable that this element in the incidence of rates has been wholly eliminated.

In its conclusion as to the effect of rates in relation to various income groups, the Hicks Report drew attention to the point that the regressive tendency of rates appeared not to be constant. There tended in fact to be periods of greater and lesser regression as family expenditure rose. This was an inevitable consequence of the basis of rating, for rates paid did not directly reflect income but varied with the rateable value of the house in which the householder lived. So long as he remained in the same house or contented himself with a house of the same rateable value, his income could rise indefinitely without thereby increasing his payment of rates. The increase would, however, arise when he decided to move to a more expensive house with a higher rateable value. It might occur from a desire to improve his standard of housing, or it might in effect be forced upon him by the need to obtain the accommodation necessary for the number of his family.

The actual burden of rates to family expenditure tends, however, to deviate from average conditions, depending on the region and local authority area in which the family lives. These variations are not a direct reflection of the rate in the £ levied, but also depend on the relationship of a number of factors, such as the level of incomes in the area, the level of rents, and the rateable value of the area, and the level of expenditure of the local authority. Since 1948 the effect of the Exchequer Equalisation Grant has been to reduce the income incidence of rates in some areas where it was high before the grant was introduced. Moreover, in those areas particularly affected by the depression before 1939 where the burden of rates was especially heavy, economic prosperity will have raised incomes and thus reduced rate incidence. The incidence of rates between areas is still, however, affected by the

<sup>1</sup> "Household Income, Rents and Rates" by H. F. Lydall and R. F. F. Dawson, *Bulletin of the Oxford Institute of Statistics*, Vol. XVI, No. 4, 1954.

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level of expenditure of the different local authorities. Such variation is inherent in a system of local government, and some difference in incidence will always remain for this reason.

## DIFFERENCES IN RATING RESOURCES

It is important to note the substantial variation between the rating resources of different local authorities. Although the differences which formerly arose as a result of variation in valuation practice as between local authorities or as between different kinds of dwelling houses should have been eliminated by the revaluation, there will remain the variation which is due to real differences in wealth stemming from the size, density and composition of population, from traditional differences in rental levels, and from the type of occupations in the areas concerned. The extent of these differences can be illustrated by a comparison of rateable value per head between different counties and county boroughs although still greater differences occur between districts within counties as the county figures are themselves averages. The following table refers to England and Wales on 1st April, 1956. The figures in brackets refer to rateable values before revaluation, on 1st December, 1955.

Counties	Rateable Value	Rateable Value per Head	County Boroughs	Rateable Value	Rateable Value per Head
Surrey ..	£,000 25,268 (15,853)	£ 18 (11)	Eastbourne ..	£,000 1,401 (995)	£ 24 (17)
Middlesex ..	40,763 (23,716)	18 (10)	Birmingham	15,849 (7,854)	14 (7)
Cardigan ..	493 (191)	9 (4)	Merthyr Tydfil ..	402 (252)	7 (4)
All counties (except London)	331,103 (194,597)	12 (7)	All county boroughs ..	187,037 (113,661)	13 (8)
All local authorities ..	622,997 (366,601)	15 (9)			

Source: *Distribution of Rateable Values between different classes of property in England and Wales.* Cmd. 9718.



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A statistical analysis and comparison of the variation in rateable values per head of "weighted" population before and after the revaluation can also be made. It is apparent from the figures in the following table that although the overall range of rateable value per head is relatively less as a result of the revaluation, when the more extreme values are discarded, the relative variation as measured by the quartile deviation is much the same.

Rateable value per head of weighted population (£)	Number of Counties		Number of County Boroughs	
	1955-56	1956-57 <sup>1</sup>	1955-56	1956-57 <sup>1</sup>
0-2.5 .. ..	2			
2.5-5.0 .. ..	35	1	15	
5.0-7.5 .. ..	20	18	52	6
7.5-10.0 .. ..	4	26	10	35
10.0-12.5 .. ..		11	4	23
12.5-15.0 .. ..		3	2	10
15.0-17.5 .. ..		2		5
17.5-20.0 .. ..				1
20.0-22.5 .. ..				3
22.5-25.0 .. ..				
	61	61	83	83
	£	£	£	£
Lower quartile <sup>2</sup> ..	4.0	7.0	5.4	8.6
Median <sup>2</sup> .. ..	4.75	8.3	6.0	10.3
Upper quartile <sup>2</sup> ..	5.6	10.1	7.2	12.3
Quartile deviation ..	0.8	1.55	0.9	1.85
Q.D. as % of median	17%	19%	15%	18%

Source: Finance Division, Ministry of Housing and Local Government, January, 1956. B.I.1454.

The revaluation has caused a far larger increase in the rateable values of some local authorities than of others. Among counties, the biggest increases have been experienced by Cardiganshire (161 per cent) and

<sup>1</sup> First estimate made in January, 1956, subject to revision.

<sup>2</sup> Extracted from the original data.

the Isle of Ely (156 per cent), the lowest by Radnorshire (19 per cent) and Cumberland (50 per cent). Of the county boroughs, the rateable value of Ipswich has increased the most (113 per cent) and that of Huddersfield the least (35 per cent). On the average, the increases in the rateable values of both counties and county boroughs in the north of England have been much smaller than in other parts of the country.

These relative differences in the size of the increase in rateable values have also affected those local authorities which are eligible to receive the Exchequer Equalisation Grant. The Grant was instituted in 1948 with the aim of securing "a substantial measure of equalisation of rates," so that all local authorities, whatever their resources, would be able to fulfil their statutory obligations to a reasonable standard. The Grant is paid to all counties and county boroughs whose rateable value per head is below the national average, and tends to be thought of as a kind of percentage grant towards all rate-borne local expenditure; the actual grant varies according to the extent to which rateable value per head of "weighted" population is less than the national average, and according to the expenditure of the local authority. (The "weighting" factors are intended to reflect the extra burden on their resources felt by certain local authorities which have a large number of children under 15 years of age, or a sparse population in relation to the mileage of roads to be maintained.) Prior to the revaluation, 54 of the 62 county councils received the grant and 55 of the 83 county boroughs. The effect of the revaluation has been to raise the rateable value of eight county boroughs above the national average, thus making them ineligible for the Grant, and to enable six county boroughs who were not previously entitled to the Grant to receive it in future. Of the counties, only one of those receiving the Grant previously has lost it. The total now in receipt of the Grant is 57 county boroughs and 53 counties.

The effect of the Grant up to now has been to narrow considerably the range of rate poundages. But the proper working of the Grant requires a uniform valuation, and now that this has been achieved, it should be possible to attain the objective of equalising rate resources more completely. Among criticisms which may be lodged against the Grant are that the method of calculation which is used (rateable value per head plus weighting factors) is inadequate to measure need, and that no account is taken of the differing resources of those local authorities which do not qualify for it.

#### THE PRESENT PROBLEMS OF THE RATING SYSTEM

Disparity between the resources of different local authorities does

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not, however, go to the root of the present problem which is why rate revenues have not grown sufficiently to meet the expanding cost of local government services. The following figures indicate the movement in rate revenues at intervals since 1913. In considering these figures it should be borne in mind that between 1913/14 and 1919/20 the general price level increased by about two and a half times, and there was an approximately similar increase between 1938/39 and 1955/56. The increase in rateable value during each of these periods was very small indeed, and the increase in rate receipts was overwhelmingly due to higher rate poundages.

Year	Rateable Value	Rateable Value per Head of Population	Rate Receipts	Rates Collected per Head of Population	Average Rate collected per £ of Rateable Value <sup>1</sup>
	£m	£	£m	£	
1913-14 ..	211.6	5.8	71.3	1.95	6/9
1919-20 ..	220.7	6.25	105.6	2.8	9/7
1928-29 ..	267.6	6.8	166.5	4.2	12/5
1938-39 ..	310.8	7.6	190.7	4.6	12/3
1946-47 ..	321.1	7.5	242.1	5.7	15/1
1955-56 ..	361.8	8.15	<sup>3</sup> 401.0 <sup>2</sup>	8.95 <sup>2</sup>	<sup>3</sup> 22/2

Source: *Rates and Rateable Values in England and Wales, 1938-39; 1955-56.*

Rates are a tax based on land and buildings and as such depend on periodic valuations if rateable value is to be kept in line with real values. There was no general revaluation between 1934 and that which has recently been made. The legislation now operative should ensure that valuations are made in accordance with the statutory provisions, on a uniform basis, and are revised at regular intervals. The valuation of houses has been continuously influenced by the national policy of rent restriction. The derating of industry and agriculture has not only

<sup>1</sup> Differs from average rate poundages because it reflects losses in collection, etc.

<sup>2</sup> Excluding payments in lieu of rates for railway, canal and electricity hereditaments.

<sup>3</sup> Estimated.



removed a large amount of rateable value from charge, but it has meant that the rates have benefited only partially or not at all from the great expansion of these two important elements in the national economy. These particular difficulties have exacerbated a general problem.

But even if these factors are remedied, the rates would still suffer from certain inherent limitations: their yield at any given poundage does not reflect changes in money incomes and they have very little natural growth. The yield of the income tax, for example, increases during a period of rising incomes without any rise in tax rates. But, in between valuations, the only "natural" increase to rateable value is from the addition of newly built properties to the valuation rolls. There can be barely any automatic increase in rate revenues, and if a greater yield is desired, local authorities must have recourse to an increase in rate poundages. Theoretically, there is no reason why rates should not be 30/- or even 40/- in the £ if the effective burden on the ratepayer is no greater because of the rise in money incomes, but strong objection is felt to constant increases in rate poundages. These objections used to manifest themselves in a psychological fear of a rate as high as 20/- in the £. Although this conception of a specific danger point has ceased to apply, the fact that some particular increase in expenditure must be found by an increase in rates causes much more widespread concern than its payment out of taxes. Lacking a natural growth, any increase in rate revenues must be sought by a rise in rate poundages and their steady increase in recent years has in fact aroused much opposition. If local government expenditure rises still further, these criticisms are likely to be accentuated as rate burdens increase. We think it right to assume that the criticisms are largely due to anomalies arising in the incidence of rates which become more marked as the reliance on rates increases.

As we have made it clear in Chapter I, we are not suggesting that the rates are unsuitable as a source of local revenue. On the contrary, we are convinced that the rates constitute an extremely valuable local tax. It is only when they are considered as the sole tax on which local authorities must exclusively rely that their disadvantages become so apparent. And it is this thought that leads us to consider alternative sources of revenue which might be available to local authorities. As a preliminary to this we now turn in our next chapter to consideration of local taxation practices overseas.

## Chapter IV

### LOCAL TAXATION OVERSEAS

BEFORE embarking on a survey of local taxation overseas, it is as well to consider what is meant by a local tax. A tax can be described as a compulsory monetary payment exacted under legal authority by a government body. This definition, however, would include payments made for specific services where the taxpayer receives an individual and particular benefit in return for his payment, as for example, fees charged for services or for licences issued. These are of special interest in a study of local revenue resources, and while they are excluded from the local taxes outlined in this Chapter, they have been separately considered in Chapter VI. For the present purpose, therefore, the taxes considered are those designed to produce revenue for general use and not related directly to a corresponding individual benefit. Thus, the English consolidated rate, although it is built up of a number of items representing the net expenditure on each of the local government services, is regarded for the purposes of this study as a tax because it is levied on all ratepayers regardless of whether or not they benefit from any particular service such as education or health. On the other hand, the charge made for sewerage services in Johannesburg, which covers the expenditure involved, is not a tax within the present definition because it applies only to those who use the service, and the amounts charged depend upon the extent to which the service is used. A borderline case is that of the licence fee which is normally charged only to cover the administrative costs involved in regulating certain selected trades; this may take on some of the features of a tax if the rate is fixed so that the revenue exceeds the administrative costs and is used for general revenue purposes.

Secondly, there is the question of when a tax is a local tax. A tax levied and collected by the central government and then handed over to the local authorities cannot in our view be described as a local tax. It is an assigned revenue and in essence no more than a government grant, the amount of which is determined by the yield of a particular tax. This is true whether the revenue is returned directly to the local authority area from which it is collected, or is distributed among local authorities according to certain other criteria. It is not necessary for the basis of a local tax to be determined by the local authority itself; in

nearly all countries, a national statute provides a universal framework for the local authorities within which they exercise a limited discretion. (One notable exception is the Netherlands where local authorities frame their own bye-laws fully governing certain taxes.) Local taxes are often assessed and collected by the local authorities, although some are not; if the assessment of the tax is a complex matter, it is likely that assessment and collection are carried out by other agencies. In the context of our approach to the whole question of local authority finance, the really vital point is the determination of the tax rate; to be a local tax in the sense we postulated, the rate *must* be determined by the local authority, even if it is subject to the approval of a higher authority or maximum and minimum limits are fixed by law or administrative decree.<sup>1</sup> There are thus degrees of "localness" in local taxation; from the tax which is defined, levied, assessed and collected by the local authority, to the tax defined, assessed and collected by the state or another public body but whose rate is still decided, within limits, by the local authority.

"Surcharges" on national government taxes are in a special category. Here the local authority is allowed to levy a percentage or *centime additionnel* as an addition to a national tax. The basis is a national tax, but since the local authority decides its own rate of surcharge, it is included here as a local tax. Among the countries we have examined, this type of local tax is used in France, Switzerland and the Netherlands.

#### LOCAL TAXATION: A COMPARATIVE ANALYSIS

The table on page 42 analyses for thirteen countries:

- (i) The relation of local to total taxation;
- (ii) The relation of local taxation to total local revenues;
- (iii) The relation of local taxation to National Income;
- (iv) The importance of different local taxes to total local taxation.

The local taxes included are, as far as possible, only those which fall within the definition given above.

The importance of local taxation to local revenues and the proportion which local taxation bears to total taxation may depend upon a number of factors which have nothing at all to do with the type of local tax levied, such as the constitutional structure of the country,

<sup>1</sup> We regard this definition as including a tax the rate of which is determined by statute or a higher authority if it is open to the local authority to decide whether to impose the tax or not.



the division of functions and fiscal powers between central and local government, the attitude of the central government towards making grants to the local authorities, or certain historical developments peculiar to a particular country. This should be borne in mind in reading the figures in the table.

It is clear from the table on page 42 that in relation to total taxation—national and local combined—local taxes are most important in the three Scandinavian countries and in Switzerland, in each case contributing over 20 per cent of total taxation and in one case over 30 per cent. In the other countries, the proportion falls steeply from 13 per cent for Western Germany, the U.S.A. and Canada to 9 per cent for the United Kingdom, 7 per cent for New Zealand and 3 per cent for Australia and the Netherlands. Norway, Sweden and Switzerland rely overwhelmingly on a local income tax; in the U.S.A. and Canada, the chief reliance is on a tax on land and buildings, but other taxes contribute between 13 per cent and 15 per cent respectively of local taxation; Western Germany is in a special position for the principal local tax is on the profits and capital of businesses and the second most important is the tax on land and buildings; in the United Kingdom, Australia, New Zealand and South Africa a tax analogous to the British local rate is the sole local tax, and it is in these countries that local taxation makes its smallest contribution to total taxation. The general position which seems to emerge is that the greater the dependence on a single local tax on land and buildings, the less important does local taxation become in relation to total taxation.

If the part local taxation plays in relation to total local revenues is examined, with one or two exceptions a similar trend appears. Of the countries levying a local income tax, only in Denmark does the proportion of local taxation to local revenues fall below 60 per cent, and Norway shows the highest percentage (68 per cent). In these countries also, local taxation makes its highest contribution to total taxation (over 20 per cent). The three countries where the percentage of local taxes to local revenues is lowest (40 per cent or lower) are also those where local taxes are the least important in relation to total taxation (under 10 per cent). In two of them, the United Kingdom and South Africa, the tax on land and buildings is the sole local tax. Australia and New Zealand are the only countries relying solely on the local tax on land and buildings where local taxation makes a high contribution to local revenues, but in both cases local authority expenditure is of small importance in relation to total public expenditure and the local taxes have therefore to meet a relatively small local expenditure.

A further analysis can be made of the relationship of local taxation

# NEW SOURCES OF LOCAL REVENUE

Local Taxation and its ... to Total Taxation, Local Revenues, and National Income

	Aus- tralia	Can- ada	Den- mark	France	Nether- lands	New Zealand	Nor- way	South Africa	Sweden	Switz- erland	United Kingdom	U.S.A.	Western Ger- many
	1952/53	1953	1953/54	1953	1953	1952/53	1952/53	1953	1953	1953	1953/54	1954	1953
I. PROPORTION OF LOCAL TO TOTAL TAXATION ..	% 3	% 13	% 25	% 11	% 3	% 7	% 28	% 7	% 31	% 24	% 9	% 13	% 13
II. PROPORTION OF LOCAL TAXATION TO LOCAL REVENUES ..	60	61	46	47	9	66	68	40	62	60	39	56	45
III. PROPORTION OF LOCAL TAXATION TO NATIONAL INCOME ..	1.3	3.6	6.0	3.1	0.9	2.3	8.7	1.2	8.5	3.8	3.1	3.7	4.4
IV. LOCAL TAXATION	100	100	100	100	100	100	100	100	100	100	100	100	100
Proportion of local taxes on													
Land and buildings ..	100	85	27	29	83	100	2	100	100	96	100	87	28
General property or capital ..							97						
Income ..			73										
Business ..		8		61									
Retail sales ..		5		3	13		*					6	69
Entertainments ..		*										*	
Poll ..		*		7	4		1		*			*	
Other ..		2										6	3

1. The sources from which the statistics are drawn are given in the bibliography.

2. In Category II (the proportion of local taxation to local revenues) the local revenues are all revenues excluding loans in some countries, while in others they are revenues on current or ordinary account. The differences, which consists largely of tax and grant revenues used for capital expenditure, is small but where it exists the percentages should not be regarded as exactly comparable.

3. The local taxes included are confined to those taxes whose rates are determined by the local authorities (sometimes within limits set by other governmental authorities). Taxes whose yield accrues to the local authorities, but where the local authorities have no discretion at all in fixing the rate or no opinion in deciding whether to levy the tax, are included as central governmental taxes, e.g., emmentments taxes in Sweden and Denmark.

\* Less than 0.5%.

## EXPLANATORY NOTES TO THE TABLE

### AUSTRALIA

- II. Local authority revenue is all revenue of local authorities excluding loan receipts.

### CANADA

In all except the comparison of local taxation to local revenues, local taxes include those taxes levied for municipal purposes and for schools, either by the school districts or by the local authorities on their behalf.

II. Local authority revenue is the ordinary revenue of local authorities and of some joint boards. Schools, hospitals, libraries and special areas are excluded.

IV. The general property tax is part of the tax on land and buildings, where that tax includes an assessment of personal property.

### DENMARK

Local taxes exclude those levied for the Municipal Equalisation Fund.

- II. Local authority revenue is revenue on current account.

### FRANCE

II. Local authority revenue is all revenue of departments and communes excluding loans. It excludes the "*établissements publics locaux*," i.e., hospitals, trade and professional organisations, and joint boards providing services for a number of communes.

IV. Local taxes exclude those parts of the turnover tax directed to the Equalisation Fund and to the departments. Business taxes include the "*patentes*."

### NETHERLANDS

Local taxes are those levied by the municipalities and provinces, and exclude taxes levied for the Municipal Fund and the Provincial Fund, and assigned tax revenues.

II. Refers to the municipalities only, and relates to the current account.

IV. One of the taxes on land and buildings contains an element of general property taxation. It is levied on the occupiers of buildings and includes an assessment of the value of the furniture in the premises.

### NEW ZEALAND

II. Local authority revenue is all revenue of counties, boroughs and town districts excluding loans, non-recurring receipts and special government grants, and the receipts of the main municipal trading undertakings.

### NORWAY

II. Local authority revenue is all revenue excluding loans and transfer payments between local authorities.

### SOUTH AFRICA

I. Estimated figure based on those given in *Official Year Book of the Union of South Africa, 1952/53*.

II. The information is based on a sample taken of 525 local authorities. Local authority revenue is current revenue for rate, housing and native administration funds. Kaffir beer funds are excluded.

### SWEDEN

II. Local authority revenue is all revenue excluding loans and capital funds.

III. Refers to gross national product.

### SWITZERLAND

II. Refers only to communes in the Canton of Zürich. Local authority revenue is revenue on the ordinary account.

### UNITED KINGDOM

I. Local tax receipts for Scotland and Northern Ireland are estimated.

II. Refers only to local authorities in England and Wales 1953/54. Local revenue is revenue on current account.

### U.S.A.

Local authorities include school and special districts. Information is exact for cities with a population exceeding 25,000, but is otherwise based on a sample of about 1,800 local government units. See also note under Canada IV.

### WESTERN GERMANY

II. Local revenue is revenue on current ("*vermögensunwirksame*") account.

IV. The miscellaneous taxes fall within the jurisdiction of the provinces, and local authorities do not in all cases possess discretion to determine the rates levied.



to national income. In the countries levying a local income tax, the relationship of local taxation to national income is 8.7 per cent (Norway), 8.5 per cent (Sweden), 6.0 per cent (Denmark), and 3.8 per cent (Switzerland). This may be compared with 3.1 per cent (United Kingdom), 3.7 per cent (U.S.A.), and 0.9 per cent (Netherlands). The proportion is higher for the first group than for the second, again showing the greater significance of local taxation in the countries where a local income tax is levied.

We cannot attempt here to analyse fully the reasons for this situation. It is interesting to note that rates in the United Kingdom contributed as much as 24 per cent of total taxation as late as 1938/39. The steep decline in importance is due partly to the great increase in overall taxation and partly to the slow growth of revenue from rates. An outline of the difficulties which the local rates in England and Wales have encountered has been given in Chapter III. There have been similar difficulties with analogous taxes in other countries, and it is generally true to say that in a period of rapidly rising prices, the local income tax is best able to hold its own in terms of yield. This is not surprising when it is remembered that a tax on income and profits directly reflects the level of money incomes and of economic activity.

In the succeeding sections of this chapter, we have reviewed the main types of local taxes found overseas. These are:

- (i) Local taxes on land and buildings;
- (ii) Local income taxes;
- (iii) Local business and sales taxes;
- (iv) Local entertainments taxes;
- (v) Local taxes on road transport;
- (vi) Local poll taxes;
- (vii) Miscellaneous local taxes.

#### LOCAL TAXES ON LAND AND BUILDINGS

The traditional local tax in most of the countries we have surveyed is based primarily on land or land and buildings, although it may also include personal property. Where a local income tax is levied, the tax on land and buildings is far less important than elsewhere. Thus in Norway, such taxes contributed only 2 per cent to local taxation in 1952/53 and in Denmark 27 per cent in 1953/54. In Sweden, the local tax on land and buildings has recently been merged with the local income tax, and to-day the annual value of property is charged as income for income tax. In Switzerland there is no local tax on land and

## LOCAL TAXATION OVERSEAS

buildings, but the communes levy a surcharge on the cantonal income tax and this includes a tax on the total property of individuals. In France, the *centime additionnel* was originally levied as a surcharge on a central government tax on land and buildings. The central government tax is no longer levied, but the *centime additionnel* continues to be levied. Dutch municipalities levy surcharges on the land and inhabited house taxes of the central government.

Land and buildings are assessed for taxation purposes either on capital value or on annual (rental) value, or, in a very few cases, on land acreage. In some countries where capital value is used, only the unimproved or site value of the land is taxed, while in others different rates are levied on land and buildings. These taxes are also in certain cases levied differentially according to the use to which the property is put. Finally, in some countries, an effort is made to tax increases in land values, the benefits property owners receive from public works, the net income received from property, and the value of vacant building sites.

The *capital value* of land and buildings is the most widely used basis of real property taxation, and is adopted by Norway, Denmark, the Netherlands (the land tax), Western Germany (for vacant land, business premises and one-family houses), U.S.A., Canada (excluding some municipalities in Newfoundland), and by nearly all local authorities in South Africa and about one in three of all local authorities in New Zealand. In five Canadian provinces personal property is included in the valuation, and in most American states the tax is nominally levied on all property, although in practice personal property largely escapes taxation.

The *unimproved capital or site value* of land is adopted as the sole basis of property taxation by two thirds of the Australian local authorities, including all local authorities in New South Wales and Queensland; about two thirds of the New Zealand local authorities; and a small proportion of the South African local authorities (chiefly in the Transvaal). In a few Canadian areas too, buildings and other improvements may be completely exempted from tax, so that only the site value is taxed.

*Annual rental value* is the basis of the taxation of land and buildings in Great Britain, Newfoundland (some municipalities), the Netherlands (the inhabited house tax), France, Western Germany (properties let as dwellings), a third of the Australian local authorities, and a few New Zealand local authorities.

One hundred and forty-eight local authorities in New Zealand value land for taxation on the basis of acreage and four on the number of sheep and cattle owned by the landowner.

Land and buildings are differentially rated in a number of countries. There are two types of differentiation between classes of property:

- (i) Differential treatment of land and of the buildings or improvements on it. In Denmark and in certain areas of South Africa and Canada, different rates are levied on the value of land and on the building or improvements on it. In the Netherlands, different rates of surcharge are levied on vacant and on built-on land.
- (ii) Differential treatment of particular types of property, such as agricultural land, farm buildings, industrial premises, or dwelling houses. This is achieved either by levying differential rates or by increasing or decreasing the valuation of certain types of property. It is practised in some Canadian provinces and some American states. In Western Germany, certain dwelling houses built since 1949 are exempt from tax for 10 years from the date of construction. Buildings completed since 1924 and houses accommodating one family are less heavily rated than older buildings and multi-family houses, and land used for business purposes is more heavily rated than other land. In none of these instances is agricultural land or industry as favourably treated as in Great Britain.

A tax on the increase in land values is levied in Denmark by the central government, and its yield, which is of minor importance, is shared with the local authorities. A few local authorities in the Netherlands tax the annual value of building sites and in France their market value. Local authorities in France may also levy a tax on the net income derived from land and buildings. In a number of countries, special assessments or benefit taxes are levied on property-owners who have or will receive benefits which are not general from public works undertaken by the local authority. These perhaps are more in the nature of charges for specific services rather than taxes for general use.

Taxes on land and buildings need periodic valuations to keep their base up to date. Such revaluations can only take place at intervals, and the new valuations often do not keep pace with rising prices. In certain countries also, an arbitrary basis of valuation has been adopted which prevents up-to-date valuations from taking place. In the Netherlands, for example, the basis of land assessment is the average value over the period 1875/81 for land which is not built on and 1892/96 for built-on land; new properties may only be valued by comparison with these values. The basis of the Norwegian tax on farm land and properties in rural districts is a division into land units last made over the period 1872/85. Property which provides the



basis for the *centime additionnel* in France is largely assessed according to the values of 1917 when the actual central government tax was abolished. In England and Wales the 1956 revaluation was based on 1939 values in the case of houses, but on current values in the case of other hereditaments.

#### LOCAL INCOME TAXES

The most important local income taxes are levied in the three Scandinavian countries. In Switzerland, local authorities levy a surcharge on the cantonal income tax. Local income taxes used to be imposed by local authorities in the Netherlands up to 1929 and in Canada up to 1941. Local income taxes have been successfully introduced in some American cities since 1940.

##### (a) *Scandinavia*

In each of the three Scandinavian countries, a long-established local income tax provides the bulk of local taxation. These taxes are essentially of the same type. In each case the income of both individuals and companies is taxed, both earned and unearned income is included, allowances may be set off against the taxable income of individuals, and there is close collaboration between the local authorities and the central government in the assessment and collection of the national and local income taxes. Among the differences between them, only Norwegian local authorities tax capital. The Danish local tax differs from the other two in that it has a progressive incidence, and the Norwegian tax at present includes a progressive surtax levied at low rates.

In *Norway*, income tax was first introduced at the local level and the first general law regulating it was passed in 1882. An income tax imposed by the central government followed in 1892. The local income tax remains the more important of the two for the majority of taxpayers and has a greater yield. Local authorities are responsible for assessing and computing both taxes, and the taxpayer files only one return. The tax is at present collected by separate agencies, but starting in 1957, the local authorities will collect both the central government and local income taxes.

The local income tax is levied on the income, both earned and unearned, and the capital of both individuals and companies; of the total assessment, in fact about 96 per cent comes from income and 4 per cent from capital. Dividends and share capital are not chargeable to tax in the hands of the individual. In addition, there is a surtax on taxable

incomes above kr. 20,000 a year; one half of its yield accrues to the local authority and one-third is paid into an apportionment or tax equalisation fund. A special tax on bank deposits and interest was abolished in December, 1955.

The individual taxpayer is assessed by the local authority in whose area he lives, but where he derives income from business activities outside his own district, that part of his income is taxed by the local authority in whose area the business premises are situated. Dividends are not taxed. There is a tax free allowance on income and capital and deductions from income are also made according to the number of the taxpayer's dependants. Rates of tax on income are proportional, averaging 17 per cent for all local authorities in Norway. (In Oslo, 16.5 per cent was levied in 1953/54.) The approval of the Ministry of Local Affairs is necessary for rates exceeding 17.5 per cent. The tax on capital is really a general property tax which includes land and buildings and other property. Share capital is not taxable in the hands of individuals. The tax is levied in nearly all cases at the rate of 0.4 per cent. The surtax on taxable incomes exceeding kr. 20,000 is levied at rates of from 3 per cent rising to 5 per cent. A government committee has recommended that this surtax should be amalgamated with the central government income tax, but this proposal has not yet been implemented. Starting in 1957, all individuals will make current payments of tax during the year in which the income is earned, and the final assessment will be made in the following year.

The income and capital of companies are taxed in the municipality where they carry on their activities, and where a company operates in more than one municipality the tax is shared between the municipalities. Companies are subject to taxation on income and capital at the same rates as individuals and they also pay the local surtax. They receive no tax-free allowances on income. Shipping companies are charged at a standard rate of tax over the whole country. The tax on shipping companies accrues to the local authorities where the shareholders live.

The central government tax on individual income and capital is levied at progressive rates. Different rates are levied on the distributed and undistributed profits of companies, and there is a proportionate tax on company capital. The combined national and local taxes on income and capital may not exceed 80 per cent of taxable income, the national tax being reduced when necessary to give effect to this maximum.

The *Swedish* local income tax is fully described in the Supplement to

this Report. The tax extends to all income, including that from property and capital (there was formerly a separate local property tax but this has now been merged in the local income tax). It is levied on both individuals and companies. The tax is not progressive. Rates vary from 7 per cent to 17 per cent (provincial averages). The rate in Stockholm is 11 per cent. The average for the country as a whole is 13 per cent. (These figures relate to 1952.) The tax is assessed on a "current year" basis and there is a system for payment on account during the year. The Norwegian plan is modelled on this system.

The national income tax is levied at progressive rates, and the local tax is allowed as a deduction from taxable income, in computing the national tax payable. There is also a national tax on capital. The total of the income, property and capital taxes may not exceed 80 per cent of taxable income. The machinery of assessment and collection is the same for both national and local taxes.

In *Denmark*, the local income tax is at present composed of four parts:

- (i) A tax on the individual in the municipality where he lives;
- (ii) A tax on the individual in the municipality where he works;
- (iii) A tax on incorporated companies;
- (iv) A tax on the estates of deceased persons.

Capital is not taxable.

In 1954 a group of bills presented to Parliament by the central government aiming at a more equitable distribution of revenue and expenditure between central and local government, included a bill to abolish the local taxes on individual income in the municipality where the taxpayer works, and on incorporated companies, with a compensating rise in the central government tax on companies. This bill has not yet been passed.

Assessment of income for local taxation is based on the assessment for central government purposes, and payments of personal tax to the central government, the Municipal Equalisation Fund, local authorities and the church are deductible. Certain family allowances are also given. The local authorities have optional powers to discriminate against certain types of income. These powers were used by less than half of the rural municipalities in 1953/54, and not at all by the urban municipalities. By this method, those parts of the taxpayer's income derived from certain sources may be increased by a percentage. Maximum percentages are laid down by law, and these are 50 per cent for



income derived from capital, 35 per cent for income from real property, 25 per cent for income from annuities, and 15 per cent for income from pensions. Lower percentages may be used, provided the same proportion is kept between the different types of income. The optional powers will be abolished if the proposed bill to reform the income tax is passed by the Danish Parliament.

The local income tax on individuals is a progressive one, and there are two methods of securing this progression. In the case of the three metropolitan municipalities constituting Greater Copenhagen, there is a fixed progressive scale of tax laid down by law. Elsewhere, the municipalities make the tax a progressive one by increasing or reducing the actual assessed income by a certain proportion, and each municipality draws up its own rules for doing this, subject to maximum and minimum limits. (The maximum increase permissible is 50 per cent.) The main criterion for increasing or decreasing taxable income is the size of the income (i.e., income above a certain level is increased), but other factors may also be taken into account. The municipalities then levy their tax rates on the computed incomes thus ascertained. Rates of tax (as between municipalities) at present vary from 4 per cent to 12 per cent.

The approval of the Ministry of the Interior is necessary to a sharp increase in the total amount of taxes raised by the urban municipalities. In the case of the rural municipalities, their local income taxes are approved with their budgets by the county councils. The tax is collected by the municipalities.

The tax on incorporated companies is levied at rates of 4 to 5 per cent on the companies' net profits, and is paid to the municipality or municipalities in which the companies pursue their activities or receive their income.

A special tax on the income and property of individuals levied at a standard rate for all municipalities and collected by them is paid into the Municipal Equalisation Fund. If the proposed tax reform bill is passed, this levy will be abolished. A surtax on those parts of taxable income exceeding a certain level will be imposed, and the proceeds will accrue to a Municipal Grants Fund. Pending approval by Parliament of this proposal, a bill was passed in 1956 as an interim measure which abolished the special tax and replaced it by an increase in the central government taxes on individual income and property.

The central government taxes the income of individuals according to a progressive scale and the profits, both distributed and undistributed, of companies. There is a general property tax, levied at progressive rates, on individuals and on foreign companies.

(b) *Switzerland*

In the 25 Swiss cantons, the communes have the right under cantonal law to levy a surcharge on the cantonal income tax. The yield of these surcharges in 1953/54 was fr. 770 million, and this actually exceeded the yield of the cantonal income taxes which amounted to fr. 741 million. Taxes levied by the Confederation on income and capital yielded fr. 318 million.

Each of the cantons has its own system of direct taxation, so that the basis of the local surcharge varies greatly. In 18 cantons both earned and unearned incomes are taxed, in two cantons unearned income is only taxed under certain conditions, and in five cantons it is not taxed at all. All cantons tax the net property of individuals, five tax the net property of companies and 20 their capital and reserves. Under the rules laid down by the Supreme Court of Switzerland designed to avoid double taxation, the income and capital of individuals are taxed in the area of domicile, and of companies in the area where the enterprise has its permanent establishment.

The communal surcharge on the cantonal income and capital taxes takes the form of a *centime additionnel*. The commune levies one or more centimes for every franc of the cantonal tax collected. The tax is assessed by the cantons with the assistance of the communes, and is collected by the communes.

(c) *U.S.A.*

The introduction of local income taxes in the U.S.A. is a very recent development. Together with a number of other new local taxes, they have been adopted with the express object of supplementing the tax on land and buildings, which has until recently been virtually the only local tax. The first local income tax came into operation in Philadelphia in 1940 and other local authorities have since followed suit. The development of local income taxes has been sporadic and unsystematic, and with the exception of Pennsylvania, they are still confined to a handful of cities in a few of the states. In 1955 a number of cities in Ohio and Kentucky and St. Louis, Missouri, and 420 local authorities in Pennsylvania (including counties, townships and school districts) levied a tax on individual incomes. Forty-eight cities imposing this tax had over 10,000 inhabitants, and ten, including five cities in Ohio, one each in Kentucky and Missouri and three in Pennsylvania, had over 100,000. The total yield for all local authorities in the U.S.A. in 1954 was \$129 million, representing 1 per cent of all local taxes. But for the individual authorities, the tax was far more important; in Louisville, Kentucky, for example, the local income tax provided 39 per cent

of all local taxes in 1952, and 25 per cent of total local revenue. The average *per capita* yield for cities with a population exceeding 10,000 was \$16 in 1955.

Individual income is taxed by all local authorities levying a local income tax, but company profits are taxed only in Ohio, Kentucky and the city of St. Louis. In Pennsylvania, the state taxes company profits and local authorities are forbidden by law to levy taxes on subject matter already taxed by the state government. In the Kentucky cities and St. Louis, citizens pay income tax to city, state and federal taxing authorities, but in Ohio and Pennsylvania there is no state tax on individual incomes.

A local income tax is also levied in Washington, D.C., but this is more akin to the federal and state income taxes; unearned income is taxed and the rate of tax is progressive. Washington in fact performs many functions which are elsewhere carried out by the state governments, and its income tax may be considered more nearly a state than a municipal tax.

All local authorities levying a local tax on income, tax the income of both residents and non-residents in so far as it is received from within the city limits, and with one exception, residents' income earned outside the city is also subject to tax. The exception is Kentucky, where the tax is called an "occupational licence tax" and is levied only on income earned within a city. Various allocation formulae are used to determine what part of a non-resident's income is earned within the city. Where many local authorities in an area levy the tax, the possibility of double taxation arises, for the taxpayer may be taxed in both the area where he works and the area in which he lives. There are two possible methods which have been adopted to eliminate this problem. In Pennsylvania, the local authority where the taxpayer lives has precedence over the local authority where his income arises, except in the case of Philadelphia which has priority under all circumstances. In Springfield and Dayton, Ohio, the local authority where the taxpayer's income arises takes precedence. Toledo, Ohio, allows taxpayers to credit payments of tax to other authorities to a certain extent against their liability to the city if a reciprocal arrangement is made.

The local authorities are responsible for the assessment and collection of local income taxes. Employers are charged to "withhold" (i.e., deduct) the tax from wages and salaries, and to pay it at monthly or quarterly intervals to the local authorities. For this reason, it is often known as a "payroll" tax. In Louisville and Philadelphia, the tax must be "withheld" at monthly intervals, or more frequently at



the employers' discretion. For all other types of income, individual tax returns must be made. Costs of collection range from less than 2 per cent to almost 10 per cent of the yield and are highest where the tax rate is low and the local authority small. The rate of tax is always proportional. The highest rate of  $1\frac{1}{4}$  per cent is levied by Philadelphia.

Local income taxes in the U.S.A. differ from the Scandinavian local income taxes in many important respects. Where they are levied, they are always imposed on individual earned income but only in some areas on company profits. Only in Washington, D.C., is individual unearned income charged to tax. Moreover, few cities allow personal or other allowances to be set off against taxable income. Nor do the American taxes extend to capital. Unlike the Scandinavian local income taxes, the American taxes are not important in relation to total taxation on income. They have been developed only recently, with the express aim of supplementing local authority revenues.

(d) *The Netherlands*

A local income tax and a local surcharge on the national income tax were abolished in the Netherlands in 1929. In their place, the central government levied on behalf of the local authorities a national municipal income tax, the yield of which was directed into a Municipal Fund. Local authorities also received powers to levy a limited surcharge on the new national municipal income tax and another on the national tax on capital. During the period 1940/45, both the national municipal income tax and the surcharges which the local authorities could levy on the income tax and on the capital tax were abolished.

In 1946, the Government set up a committee of enquiry (Oud Committee) with strong local government representation on the question of the proper division of responsibility and of financial burdens between the central government, the provinces and the municipalities. This committee has issued a number of reports and one of the latest of these, published in November, 1954, deals with the question of a local income tax. A fully-fledged local income tax was rejected on the grounds that the central government already dominated this field, and that any additional local tax on these lines would make the total burden of direct taxation too heavy. A majority of the committee, however, recommended the introduction of a municipal residence tax (*woonplaatsbelasting*) which it was felt would assist in restoring a sense of financial responsibility to the municipalities and to their citizens. The tax would be levied by the municipalities on citizens living in their areas on the 1st January of each year. The basis would be the income of the taxpayer, after deduction of the income

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tax payable to the central government by a bachelor (i.e., the highest possible deduction), and the tax on capital. Further deductions of fl.800 for unmarried persons, fl.1,200 for married persons and fl.1,300 for each child would be allowed. The municipalities would have discretion to levy rates of from 1 to 3 per cent on the assessment thus reached. Assessment and collection would be carried out by the municipalities on the basis of information supplied by the central government administration. It was estimated that the tax would yield between fl.45 and fl.135 million in 1952/53 (approximately 3-9 per cent of local revenues) or fl.13-14 per inhabitant (about 27/-). It was suggested that it should be introduced at the same time as the proposed reduction in the central government income tax.

A minority of the committee opposed the proposal on the grounds that the incidence of the tax would be inequitable as between individuals living in "rich" and "poor" areas, and that it would be expensive to administer in comparison with the national income tax which is withheld at source from wages and salaries. They furthermore thought that considerations of national economic policy did not permit the introduction of such a tax.

The Oud Committee's proposal for a municipal residence tax is supported by the Netherlands Union of Local Authorities. It is now being considered by the Government, and the Minister of the Interior has said that the tax might be of value to local autonomy provided it is combined with grants from the Municipal Fund which would meet the needs of individual local authorities, and with a system of specific grants from the central government.

## BUSINESS AND SALES TAXES

The most important business taxes are levied in Western Germany, France, the U.S.A. and Canada, while retail sales taxes are used in the two latter countries, in some cases by the same authorities that levy business taxes. The most widespread local charge on business is the simple licence fee levied at a flat rate with different rates for various types of business. These licences are usually introduced to control and regulate business activity in a local authority's area, and are often charged at a rate merely designed to cover the administrative costs involved. These licence fees are therefore not necessarily taxes in the strict sense. There are, in addition, business taxes intended to produce revenue for general use. These are of several types. They may be additions to the property taxes on business premises. Some are akin to the local income taxes on companies, while others have developed from a licence fee into a tax on gross receipts which is an attempt to

## LOCAL TAXATION OVERSEAS

measure the volume of activity of the business. The number of employees, the number of machines used, and the value of the premises are other factors which may be used to determine the liability of a business to tax. Although many business taxes are similar in kind to other local taxes, they are all included here as business taxes because they are separately levied on business enterprises. A further type of business tax is the sales tax levied on products at the retail level.

### BUSINESS TAXES

#### (a) *Western Germany*

The business or trade tax levied by all municipalities in the West German Federal Republic is currently the most important of the local taxes there. Over the last eight years, it has outstripped the land tax in terms of yield and contribution to local taxation. In 1953 it yielded over D.M. 2,500 million, or 69 per cent of local tax receipts. In structure it is similar to the Scandinavian local income taxes which tax companies as well as individuals.

The basis is the taxable profits and taxable capital as defined for provincial (*Land*) income tax purposes of all industrial and commercial companies and all individuals carrying on a trade except farmers. The assessment of profits is made by the provincial tax collection office advised by a committee of local representatives, and would normally differ little from the assessment for provincial income tax purposes. The valuation of capital is carried out according to the Federal Valuation Law by which all property is valued. A percentage of between 1 and 5 per cent of taxable profits and of 0.2 per cent of taxable capital is then calculated and these added together form the tax base. There is a tax-free allowance of D.M. 1,200 on the profits of unincorporated businesses, and of D.M. 6,000 on all capital. The tax levied by the municipalities is then computed by multiplying this tax base by a factor which varies from 2 to  $3\frac{1}{2}$  times, subject in some provinces to a maximum set by provincial legislation. The tax is collected by the municipalities.

In addition, in certain provinces the municipalities may, with the consent of the provincial authority, levy a payroll or salaries tax. This is usually done when labour is especially important in the enterprise, and is accompanied by a reduction in the rate of the tax on profits and capital. The rate, which may be as high as a factor of 10 in the case of this tax, is applied to a tax base which is a percentage of 0.2 per cent of the monthly salary payroll. The tax is paid by the employer.

#### (b) *France*

There are three types of business taxes at present levied by local



authorities in France. They have become increasingly important in French local finance in recent years and in 1953 contributed some 60 per cent of total local taxation.

(i) Up to April, 1955, the most important of the business taxes was the additional tax (*taxe additionnelle*) levied on the central government's turnover tax. It was based on the total of all sales of goods at the wholesale and retail level, and on services rendered, but not on the wholesale sales of produce by the producers. Sales of certain essential commodities such as bread, milk and newspapers were exempt from tax. Between 60 and 75 per cent of the tax, which was collected by the central government, went to the communes, 15 per cent to the departments, and the rest to the Equalisation Fund. The discretion of the local authorities to vary the rate of tax was very limited. The rate levied on most types of goods was laid down as 1.5 per cent, but the communes could increase this to 1.75 per cent if they wished. A higher rate of 2.7 per cent was levied on retail sales where the owners had more than two retail shops, or where they sold concurrently for wholesale and retail and the wholesale transactions exceeded a third of the total turnover. The communes could increase this rate to 3.2 per cent. The departments levied the tax at the basic rates.

In 1955, the central government, exercising special powers granted by Act of Parliament, issued a decree abolishing the additional tax on turnover together with the central government tax on which it was levied. Instead of a local tax (*taxe locale*) was introduced as part of a new system of turnover taxes. In general, the basis of the new tax is the same as the old turnover tax on which the surcharge was levied, but there are certain changes. The rates of tax are now 2.65 per cent for the normal rate, which the departments may increase to 2.75 per cent and the communes may reduce to 2.2 per cent; this applies to all sales for resale, to retail sales, wholesale sales liable to the central government tax on value added where the taxpayer opts to pay the local tax, certain services, and deliveries by co-operative societies. A higher rate of 8.5 per cent is levied in certain cases. The sale of bread, milk, newspapers, exports and transactions affecting goods destined for agricultural use are all exempt from tax. Certain commodities, such as petrol, which is taxed by the central government, meat and cattle food, lie outside the field of the tax.

(ii) The *patente* or business licence is one of the four fictitious principals on to which the local authorities may levy a surcharge or *centime additionnel*. For every franc that the central government levies, the local authority levies one centime ( $\frac{1}{100}$ ). It is levied on all occupations

and trades except farming and self-employed artisans. The basis of the principal consists of two parts: a fixed fee which varies according to the type of business or profession, the number of workers employed, the number of machines used, and the population of the commune in which the enterprise is situated; and a proportional charge which is based on the rental value in 1947/48 of the premises used.

In 1955 the central government issued a decree under special powers granted by Parliament to modify the *patente*. The proposals will come into force in 1957. The proposed changes are modelled on the system in use in the three departments of Alsace-Lorraine which will be extended to all departments in metropolitan France. The number of employees in the business will become the most important element in the fixed charge which is part of the tax base. The fixed charges will be revised periodically.

(iii) An optional tax on the rental value of premises used for professional purposes may also be levied by local authorities. The basis is the valuation used for the base of the *patente* (see (ii) above). This tax is of very minor importance.

An attempt to reform the local tax system more radically was made in November, 1953, when the French government introduced a bill which proposed to replace the system of *centimes additionnels* by three new direct taxes of the type at present levied solely by local authorities in the three departments constituting Alsace-Lorraine. One of the taxes was to be a tax on all occupations, professions and business enterprises, including farmers. It was to be based on an assessment of the productivity of the enterprise, which was to take into account such factors as the type of occupation, the rental value of the premises, the materials used in production, the number of workers employed, etc. In the case of farmers, the basis was to be solely the rental value of their land. The draft bill met with considerable opposition from the farmers and was not passed into law.

#### (b) U.S.A.

Business taxes in the U.S.A. have developed from the fixed charges for licences which were, and are still, widely used to control business enterprises. Some cities license only those businesses which require regulation or supervision, while others license nearly all classes of business. More recently, licence fees have been expanded into gross receipts taxes on all or some types of business to meet the growing need for increased municipal revenues. (189 cities with a population exceeding 10,000 levied gross receipts taxes in 1956.) The basis of

the tax is the gross receipts or turnover of the business. Some local authorities levy their rates directly on this sum, but others seek to measure liability more carefully by, for example, imposing lower tax rates on businesses with narrow profit margins. The rates of tax are generally under 1 per cent.

A very common form of business tax is levied on companies supplying utility services, such as gas, electricity, water and telephone services. Taxes of this kind were levied by 341 cities with a population exceeding 10,000 in 1956. The tax is commonly levied on gross receipts, and the rates range from 1 to 10 per cent. Some local authorities impose the levy upon the consumer, turning it into a limited form of sales tax.

#### *(d) Canada*

In all Canadian provinces except Prince Edward Island, local authorities may levy taxes on businesses. Receipts contributed 8 per cent to total local taxation in Canada in 1953. The kind of tax most widely adopted is that levied on the rental value of premises occupied for business purposes. Rental value is taken to be the actual rent paid, and the rate of tax levied may be uniform or may vary with the type of business. In Ontario and in two or three cities in the Maritime Provinces, the tax is really an addition to the property tax, the rate of which is levied on a percentage of the property tax assessment. This percentage varies with the nature of the business; wholesalers tend to be taxed at a higher rate than manufacturers, and retailers at the lowest rate. A cruder form of business tax is used in Saskatchewan, where the property tax rate is levied on an assessment based on the area of the business premises, weighted according to the type of business. Finally, Saint John, New Brunswick, levies a tax on a percentage of the turnover of retail and wholesale businesses, the percentage again varying with the nature of the business. Special taxes are also levied by some authorities on companies supplying utility services. These may be flat charges, or based on the amount of service supplied. For example, bus companies may be taxed on the number of buses, telegraph companies on cable footage, etc.

#### *(e) Switzerland*

Mention may also be made of the tax on occupations levied by communes in the canton of Geneva, in addition to the surcharge on income and profits. This is imposed on both individuals or companies engaged in any business or profession, with the exception of farmers. The tax is based on a number of factors, namely turnover, the rentable



## LOCAL TAXATION OVERSEAS

value of the premises of the business, the number of employees and the materials used. There are 34 possible tax classes depending on these factors.

### RETAIL SALES TAXES

#### (a) *U.S.A.*

In ten American states some 900 cities levy local sales taxes (171 with a population exceeding 10,000 in 1955). In most of these states, there is already a state sales tax. Local sales taxes are most widely imposed in Illinois and in California, where they are adopted by over half of the cities including Los Angeles, San Francisco and Oakland. New York City, Chicago, Washington, Denver and New Orleans are large cities which also impose local sales taxes. Local sales taxes are generally imposed as a percentage of the retail sale price of all products other than those intended for resale, and are paid by the purchaser to the retailer, from whom they are generally collected by the local authority. Certain goods and services, such as food products, are not taxed. Rates of tax vary from 3 per cent in New York City, where there is no state sales tax, to  $\frac{1}{2}$  per cent in some of the Californian cities where the state levies a sales tax of 3 per cent.

Selective excises on particular goods are also imposed by local authorities in the U.S.A., namely on motor fuel, cigarettes and tobacco, and liquor.

#### (b) *Canada*

Montreal was the first city to adopt a retail sales tax and was followed by Quebec in 1938. To-day the tax is used by many cities in Quebec province, accounting for some 15 per cent of Canada's total population. The province of Quebec adopted its own sales tax in 1940, and the local taxes are to-day collected by the provincial government along with its own tax of 2 per cent and returned to the local authorities.

### ENTERTAINMENTS TAXES

Local entertainments taxes may be levied in six of the twelve countries here surveyed, namely in Switzerland, France, Norway, the Netherlands, the U.S.A. and Canada. The Swedish entertainments tax, although it is administered by the local authorities, is charged at rates determined by the central government, with whom the yield is shared. It is not therefore, strictly speaking, a local tax in the sense we have defined it. The same is true of the entertainments tax in Western Germany, the provinces generally being responsible for determining the rates, although the municipalities exercise considerable discretion

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in deciding which entertainments qualify for a reduction in the tax rate under the provisions laid down in the provincial laws. Local entertainments taxes may be adopted by local authorities in two Canadian provinces (Saskatchewan and Newfoundland) and seventeen American states. In the Netherlands, all but the smallest municipalities impose an entertainments tax. With the exception of the Netherlands, the local entertainments tax does not make a sizeable contribution to total local tax receipts in any of the countries quoted.

The usual method of imposing this tax is by making a charge on admission tickets. There are usually certain exempted classes of entertainment on which tax is not charged. Entrance-free entertainments, educational and cultural entertainments and charity performances may fall within the scope of exemptions allowed. Further reference to the entertainments taxes levied in the Netherlands and Western Germany is made in Chapter VIII.

### ROAD TRANSPORT TAXES

Taxes on motor fuel and motor vehicles are levied by many local authorities in the U.S.A. Motor fuel taxes, which are already levied by the federal government and by most states, are also imposed by local authorities in five states, at an average rate of about 1.2 cents per gallon. Motor vehicle taxes are levied by local authorities in 15 states, but are most widely used in Illinois, where limits are set by the state to the rates which may be levied on different types of vehicles. Mention may also be made here of parking meters which are widely used in the cities of the U.S.A. and which often yield a substantial sum for general revenue purposes. They are also used in Stockholm, Auckland and some cities in Western Germany.

### POLL TAXES

Poll taxes are levied in five of the Canadian provinces, but most notably in New Brunswick where they contributed 16 per cent of all local taxes in 1953. Normally all adults are liable (sometimes only men) living in the area who have paid no other local taxes. In a few cases, the rates of tax are graduated. In Switzerland, the general poll tax is a flat rate levied on all resident adults, but in some cantons there is an additional tax on householders. Poll taxes are also levied by some cities in the U.S.A.

### MISCELLANEOUS TAXES

There are a number of licences and other local taxes which may be mentioned. Licences for dogs, licences for the sale of spirits, and stamp

duties are among them. In addition, particularly in the Netherlands, Switzerland and France, there are a variety of optional minor taxes yielding a small revenue for a few local authorities. These include a tax on advertisements (Netherlands), on hotel bills (Switzerland and U.S.A.), on gains from the sale of real estate (Switzerland), on hunting rights and on all beverages consumed in restaurants or cafés except beer (Western Germany), and on hunting rights, horses and carriages, spa waters, furnished lodgings, personal servants, clubs, balconies and musical instruments (France).

#### CONFERENCE ON LOCAL FINANCE AND LOCAL AUTONOMY

At a congress in Rome in September, 1955, the International Union of Local Authorities considered local government finance and its relation to local autonomy. The report<sup>1</sup> before the Congress, which collated the practice of 24 countries, and the discussions at the sessions, brought out much that is familiar to students of English local government finance such as the anxieties of local authorities about their decline in importance *vis à vis* central governments, the relative inelasticity of local sources of revenue, increasing financial dependence on the central government, and the growing central control which dependence naturally brings. Pleas were made for adequate local sources of revenue free from state control and for local government to have a voice in the distribution of any central subventions. The latter should as far as possible take the form of unconditional grants instead of grants for specific purposes to which meticulous conditions are so often attached.

Of special significance for this report was the two-way classification of local authorities. Local authorities were first broadly classified according to the proportion of *total* government expenditure which is incurred by *local* government. There were three classes: greater than the norm, within the norm, and less than the norm. Local authorities in Great Britain were in the middle class, i.e., they had an average share in total governmental expenditure. Next, countries were grouped according to the proportion of expenditure which their local authorities derived from their own taxes: high, average and low. Great Britain fell into the last class, a position explained by our dependence on a tax on land and buildings. The only countries who depended on a single tax and yet fell into the first class, i.e., derived a high proportion of their incomes from their own resources, were the Scandinavian countries (excluding Denmark). There the single tax takes the form of a long established local income tax.

<sup>1</sup> See Bibliography.



Most significant of all perhaps was the fact that the countries whose local authorities had the greatest proportion of independent revenues were in the main those which did not record dissatisfaction with the local government system. The Swedish report, for example, said "the financial system does not hamper the healthy development of local government activity."

The report of the Rome Congress brings home the unenviable position of Great Britain—in only four of the 24 countries did local authorities derive a smaller proportion of revenue from their own resources. At the same time it made clear the healthier and happier state of affairs where local authorities are not so beholden to the centre for money.

## Chapter V

### MODIFICATIONS AND IMPROVEMENTS IN THE EXISTING RATING SYSTEM

THE rating system as such is not within our terms of reference, and we have not regarded it as appropriate, or indeed possible in the time at our disposal, to embark upon a detailed examination of it. But, before we came to consider proposals for new types of local taxes, we felt it desirable to look at various proposals which have been made for modifications in the rating system to see if they were likely to yield a substantial increase in the revenue from rates. Schemes for the reform of the rating system are numerous; many set out to improve the incidence of rates between classes of property and between individuals. Our purpose, however, was to find further sources of revenue for local authorities, and we looked at such schemes principally with that aim in mind. This does not imply that proposals for the reform of rating which do not result in increased revenues are unimportant, but simply that they fall outside the sphere of the present study. In the following paragraphs we deal with four of the suggested modifications in the rating system, namely:

- (a) The withdrawal of derating;
- (b) Site value rating;
- (c) Capital value rating;
- (d) Rating of unoccupied sites and buildings.

#### WITHDRAWAL OF DERATING

From our point of view, the proposal for the withdrawal of derating from industry and agriculture, either wholly or in part, is the most important of these schemes. Administratively this proposal gives rise to no great difficulty, and it requires no radical change in the system. Although, in some of the other countries that we have reviewed, taxes on land and buildings are made to bear more heavily on some kinds of property than on others, in none of them is agricultural land or industry derated to anything approaching the same extent as in Great Britain.

The rateable value of agricultural land was reduced for purposes of rating by 50 per cent in 1896, and by a further 25 per cent in 1923; in 1925 relief was also extended to agricultural buildings. In 1929 agricultural land and buildings were totally exempted from rates, and the principle of derating was for the first time extended to industry. Industrial hereditaments were to be rated on 25 per cent of their annual value, and freight transport on 25 per cent also. This position still obtains to-day, except that since 1948 railway and canal hereditaments have been removed from the valuation lists, and payments in lieu of rates, based on 25 per cent of rateable value, are made by the British Transport Commission to the Ministry of Housing and Local Government for distribution to the local authorities.

In England and Wales, the reductions in rateable value under the derating provisions amounted in April, 1956, to £106 millions for industry and £3 millions for freight transport (excluding the value of hereditaments for which payments in lieu of rates are made by the British Transport Commission). At an estimated average rate poundage in 1956-57 of 15s. 8d.,<sup>1</sup> derating represents the equivalent of about £85 millions of rate revenue.

No exact calculation of the loss of rateable value due to the derating of agricultural land and buildings can be made, as agricultural land has not been assessed since 1930. An estimate was, however, made recently by the Society of County Treasurers,<sup>2</sup> based on the net annual values in 1930, with adjustments (up to 1951) for the estimated loss of land for housing and for the increase in the level of agricultural rents. This suggests that full rerating would add £37 millions to rateable value, and rerating on 25 per cent of net annual value (the position between 1923 and 1929) £9 millions. At an estimated average rate poundage of 15s. 8d. in 1956-57, this is the equivalent of £29 millions in rate revenues with full rerating and £7 millions with partial rerating.

The total amount of money lost to the local authorities by derating may therefore be put at something like £115 millions. This figure does not allow for adjustments in rate poundages which might follow an increase in rateable values due to derating.

We recognise that derating was introduced to help industry and agriculture during a period of trade depression. Its continuance after these conditions have ceased to exist has deprived local authorities of the full benefits which many would otherwise have enjoyed from the

<sup>1</sup> The actual average rate poundage is not known at the time of going to press.

<sup>2</sup> Society of County Treasurers, *Abrogation of Present System of Derating, A Report to the County Councils Association*, 1954.



## MODIFICATIONS & IMPROVEMENTS IN THE EXISTING RATING SYSTEM

expansion in the national income and from the growth of agriculture and industry in recent years. The loss of this income has been a particularly important factor in raising to such a high point the dependence upon grants of a number of local authorities. We realise that a decision about the future of derating may depend largely upon considerations which lie outside the field of this study. As a matter of local government finance and as a means of reducing the dependence of local authorities on government grants, we recommend its abolition. If, for reasons of national policy, subsidies for agriculture and industry are held to be necessary, we feel very strongly that such provision should be made entirely from the National Exchequer.

### SITE VALUE RATING

Under most systems of site value rating, real property is assessed on its capital value based on market selling prices, but the improvements or buildings are derated and the rate is thus levied only on the land or site; for this reason, it is often called a rate on the unimproved capital value of land. In Australia all local authorities in New South Wales and Queensland, all rural authorities in Western Australia, and some local authorities in other states, levy rates based on unimproved capital values: for the country as a whole, nearly two-thirds of the local authorities (covering 92 per cent of the total area under local government) levy rates on unimproved capital values. About one in three of local authorities and *ad hoc* boards in New Zealand rate on site values and about one in ten in South Africa (almost exclusively in the Transvaal), while others levy different rates on land and improvements. In the western provinces of Canada, local authorities exempt improvements from rating, usually to the extent of one-third of their value. Of the European countries surveyed, only in Denmark is a form of site value rating used; here separate rates are levied on land and on improvements, the latter bearing a lighter burden. The tax on land values, which developed from a "fertility" tax on land known since the seventeenth century, operates successfully. There is also a minor tax on the increase in land values imposed since 1932 and aimed to curb land speculation. In the countries where site value rating is adopted it appears to be successful, but it should be noted that of the countries surveyed in this Report, with the single exception of Denmark, it is used in countries of extensive land areas and new urban development.

Many arguments are advanced in favour of site value rating. Firstly, it is said that a site value rate encourages the development of land, because improvements are not rated at all while the site is taxed and

it thus pays the landowner to develop his land. Secondly, the site value rate enables the community to tax the gains accruing to the owner of land which, by virtue of inherent or outside factors, may appreciate greatly in value. For example, a site on the edge of an expanding town will have a developmental value far above its existing use value as agricultural land, and a site value rate will reflect this. Thirdly, it is suggested that the site value rate is borne by the owner and not the occupier. Finally, with site value rating, vacant building plots may be rated. We accept the argument that site value rating encourages the development of land. For that reason it is a useful tax, especially in an expanding country with a large area of land, but it is of less interest to a country like Great Britain where planning regulations are aimed at controlling the development of land at the proper pace and for suitable purposes. It is also true that site value rating taxes the development value of land, and it would admittedly be desirable to tax gains resulting from community development; but this could equally be achieved by a rate based on the capital value of both land and improvements, or by a capital gains tax. We consider, however, that it is a fallacy to suppose that the landowner bears the whole burden of the site value rate. As with annual value rating, the owner will pass on to the occupier as much of the rate burden as market forces of supply and demand will permit. Vacant sites may easily be taxed by other means than a site value rate. Finally, in very many cases the site value rate would come out of the same pockets as the present rate it supplemented, e.g., in the case of owner-occupiers, municipal house tenants, industrial concerns and others owning their own premises. On examination then, the advantages to be derived from site value rating in Great Britain appear to be limited.

The possibility of rating site values in the United Kingdom was the subject of an enquiry by a government committee which reported in 1952.<sup>1</sup> A majority of the committee came to the conclusion that site value rating was neither practicable nor desirable. A minority of three, however, supported it in principle and thought that it could be worked even with the existence of development charges under the Town and Country Planning Act of 1947.

The majority report of the committee found serious difficulties in the valuation of sites for rating. It was pointed out that, in practice, valuation is based on assessment of the full capital value of site and improvements. The site value can then be ascertained either by

<sup>1</sup> Ministry of Housing and Local Government and Scottish Home Department, *Report of the Committee of Enquiry on the Rating of Site Values* (Chairman: Erskine Simes, KC), 1952.



valuing the buildings and deducting this from the total (the "residual" method), or by assuming a more or less arbitrary relationship between site and improvements and dividing the valuation accordingly (the "apportionment" method). The committee's conclusion was that such an assessment was bound to be artificial, would not be understood by the ratepayer, and would therefore probably be disputed by him. Moreover, site valuation would make further demands on the limited number of trained valuers available.

On the assumption that the value of a site was between 20 and 50 per cent of the value of a total hereditament, the majority report estimated that the assessment of sites might add between £100 millions and £300 millions to the then rateable values in England and Wales. This estimate was based on the assessment of annual values used for income tax and rating purposes, with allowance for the possibility of under-assessment. Site value rating is usually conceived as a supplement to full rating. In this case, with a rate of 2s. in the £ (as was suggested in the Bill presented to Parliament by the LCC in 1938-39), the yield of the rate would be in the region of £10 millions to £30 millions. This is not a very large sum in relation to total revenue for rate fund services of £992 millions in 1953-54. If, however, a site value rate were conceived as a substitute for the existing rating system, it would be necessary to raise approximately £401 millions (the yield of rates and payments in lieu of rates in 1955-56) from the assessed values of sites alone. The rate poundages to be levied would depend on what the rateable value of sites turned out to be, but taking the estimate made by the committee in 1952, i.e., between £100 millions and £300 millions, the average rate poundage for England and Wales would be anything from 27s. in the £ on a basis of £300 millions to 80s. in the £ on a basis of £100 millions. With a rate of tax at this level, the anomalies of a system with such a narrow base would be grossly accentuated. The recent revaluation would suggest higher figures for site values than those given above with corresponding increases in the yield of a site value tax. There is no reason to suppose, however, that this would be so great as to invalidate our general conclusions.

As a supplementary measure, site value rating is not likely to yield a great deal of revenue. As a substitute to the present rates, it would probably have to be imposed at very high poundages. In either case, the problems of valuation might well lead to serious difficulties, and the higher the rate of site tax, the greater the injustices which would arise in the incidence of the tax. We believe that any advantages to be derived from site value rating could be obtained in large measure



with other methods of rating. Our conclusion is therefore against a site value rate.

#### CAPITAL VALUE RATING

Capital value rating with liability on the owner and an assessment of land and buildings based on capital values, yields many of the advantages outlined in the previous section. The "developmental" value of property is reflected in the assessment, which is based on market selling prices, and vacant sites are rated. The full development and use of properties is thus encouraged. The valuation of owner-occupied property is more truly in accordance with real values than is the case with assessment on an annual value basis, and the actual valuation in these cases would give rise to fewer difficulties. The system is thus particularly suitable where there is a large proportion of freehold property.

Capital value rating is in fact employed by local authorities in Norway, Denmark, the Netherlands (the land tax), Western Germany (for certain types of property), the United States, Canada (excluding some local authorities in Newfoundland), South Africa, and by some local authorities in New Zealand.

In England and Wales the basis of rates has always been occupation, and as lettings were common, valuation was based on annual value or effectively on rents. Formal liability is to-day on the occupier. With a prevalence of tenant occupation, and provided there is a reasonable proportion of free rents for evidence of rental values, annual value rating is in our view likely to be more accurate on the whole than capital value rating. The latter depends to a far greater extent on judgment than on existing use. The present problems of valuation in England and Wales are due primarily to rent restriction, which removes much of the evidence of free rental values; before rent restriction, apart from certain special cases, there were no inherent technical problems in valuation according to annual values.

A changeover from the established system of rating on annual values to one based on capital values, with all the implied disturbances and rearrangements, would have to be justified in terms of greatly increased revenues, or of very considerable other advantages. While it is difficult to estimate the effect on revenues if capital value rating were substituted for annual value rating, a large gain would seem to be unlikely. We suggest that the other probable advantages, chiefly the possibility of taxing developmental values to a greater extent, are insufficient to justify this major change.

## MODIFICATIONS & IMPROVEMENTS IN THE EXISTING RATING SYSTEM

### RATING OF UNOCCUPIED SITES AND BUILDINGS

One improvement which could, in our view, be made in the existing system is the whole or partial rating of unoccupied sites and buildings. The owners of unoccupied properties benefit from certain local authority services, and there is therefore a strong argument that they should contribute towards them.

## Chapter VI

### FEES, RENTS, RECOUPMENTS, ETC.

In this Chapter we examine the income of local authorities from fees, rents, recoupments, etc., and the possibilities of deriving additional income from these sources. The total income derived from this source is far from negligible. In 1953-54 it amounted to some £186 millions, of which housing accounted for £86 millions. The proportion which this income bears to total rate fund expenditure has, moreover, steadily increased from 10 per cent in 1913-14 to 16 per cent in 1938-39 and 19 per cent in 1953-54.

The income derived by local authorities from this source consists of charges made for particular services, rents from municipal housing and other local authority property, "recoupments" or payments from other public authorities for services rendered, sales of goods such as by-products or surplus material, licence fees, and other sundry income. There are, in addition, the profits from municipal trading services which are transferred to the rate fund to be used as general revenues, amounting to £1.6 millions or 0.2 per cent of total revenue in 1953-54.

Local authorities derive their powers to charge for services from the Acts of Parliament under which the services are provided, and the statute may set limits to such charges or otherwise circumscribe the powers of local authorities. Considerable latitude is, for example, given to the local authorities under the Public Health Act of 1936, which empowers them to make reasonable charges for removing trade refuse and to charge as they think fit for cleansing cesspools at the request of the owner or occupier of premises where there is no obligation to do so. On the other hand, the power of the local authorities to make charges under the National Health Service Act of 1946 is far more restricted. Reasonable charges may be made for services to prevent illness or ensure after-health, but the local authority must have regard to the means of the person receiving the service, and such charges are subject to the general approval of the Minister of Health.

The percentage of gross expenditure on local services met by fees, rents, recoupments, etc., varies greatly from one service to another. The following table illustrates these differences in regard to a number of services, the classification being that adopted in the published



# FEES, RENTS, RECOUPMENTS, ETC.

*Local Government Financial Statistics* for 1953-54. It will be appreciated that a service in this list may be made up of a number of distinct functions and that, within a service, some of the functions may be provided without charge while a charge may be made for others. A complete analysis would require the inclusion of a disproportionate amount of detail, but the examples given below will illustrate the considerations which arise in regard to a number of the major services.

## PERCENTAGE OF GROSS EXPENDITURE ON LOCAL SERVICES IN ENGLAND AND WALES MET FROM FEES, RENTS, RECOUPMENTS, etc., 1953-54

<i>Less than 10%</i>	<i>10%—40%</i>	<i>Over 40%</i>	<i>Full recovery</i>
Education	Refuse removal	Baths, washhouses, etc.	Small dwellings acquisition
Libraries and museums	Care of aged, handicapped and homeless	Housing	Private street works
Individual health services	Town and country plan- ning	Allotments and smallholdings	
Sewerage	Weights and measures	Registration of births, etc.	
Protection of children	Parks, etc.	Emergency residual services	
Highways and bridges			
Public lighting			
Fire service			
Police			
Civil defence			
Land drainage, etc.			
Administration of justice			

Source: *Local Government Financial Statistics*, 1953-54

The different considerations which arise in regard to fees, rents, recoupments, etc., are illustrated by the following examples:

- (i) Of the total income of £186 millions, no less than £86 millions is derived from receipts shown in the housing revenue accounts, i.e., in effect from the rents of municipal houses. The expansion of municipal housing has been responsible for the increase in the percentage which income from fees, rents and recoupments bears to the total income of local authorities. Local authorities

are free to determine the rents which they charge for their houses. The whole course of municipal housing has, however, been governed by the conception that from time to time there will usually be a gap between the cost of providing and maintaining the houses and the rents which are reasonably obtainable from the tenants, and that this gap will be met by contributions from the rates and from government grants, the basis and amount of the latter having been determined by Parliament under a number of different Acts.

- (ii) It will be seen from the first column of the table that in a number of local government services the amount of revenue received covers only a small proportion of the cost, and that this applies to a number of the largest and most important services, such as education, individual health, the protection of children, sewerage, highways and bridges, police and fire service. In effect these services are free to the individual user, and the cost is borne by the general body of ratepayers, assisted in most cases, though not in all, by government grants. It can broadly be said that for services which benefit all ratepayers to a greater or less extent, it has long been general policy to spread the charge over all ratepayers on the basis of rateable value without regard to the degree of individual benefit. The tendencies of recent policy appear to have been to extend this policy to services which benefit some ratepayers, as manifested by the extension of free education to include secondary as well as primary schools, and by the limitation on charges for those local government services which form a part of the National Health Service. The existence of some revenue from these services arises from the fact that charges are made in respect of particular functions in what are basically free services. Thus, although primary and secondary education is free, charges are made in respect of school meals. In the infant welfare service, no charges are made in respect of the medical and nursing service, but charges are made in respect of infants' foods which are obtainable as part of the service, and in respect of home helps provided after confinements at home.
- (iii) In the services included in the second and third columns of the table, a larger proportion of the cost is covered by income received from payments made for the use of the services. But these services are not homogeneous. Services provided for the care of the aged, handicapped and homeless are for the benefit



#### FEES, RENTS, RECOUPMENTS, ETC.

of particular groups of people, and the amount of the charges made for the services is broadly determined by considerations of social policy. Services such as baths, washhouses and parks are available for all members of the community, and the amount of revenue depends on the views of local authorities as to the charges it is reasonable for them to make for their municipal services or particular aspects of them. In the case of refuse removal, there is a clear distinction between domestic and trade refuse, charges being made for the latter while the cost of the former is spread over the whole body of ratepayers without regard to the degree of individual benefit.

- (iv) The fourth column of the table includes services in which it is contemplated, as a matter of policy, that the full cost of services will be recovered from the beneficiaries, and the published statistics indicate that this objective is in fact secured.

#### CHARGES FOR SERVICES

Whether any change is likely to take place in the future in the amount of income received from charges for services will depend on a number of factors:

- (i) The distribution of the weight of local government services between those which are free and those which are the subject of charges.
- (ii) The extent to which charges are in effect prescribed by the central government.
- (iii) The attitude of local authorities themselves towards charges where they are empowered to make them and where the amount of the charge is left to their own discretion.

Charges for services play a more important part in local government in other countries, and are particularly significant in South Africa. In Johannesburg, for instance, £3 millions or 39.1 per cent of the total income was derived from charges for goods and services in 1952-53 compared with 15.4 per cent in Birmingham and 14.5 per cent in Coventry in 1954-55. (In both cases, housing and the major trading undertakings are excluded.) It would be unwise to attach too much importance to a comparison of the gross figures, but it may be observed that substantial sums are derived from services from which little income is received in this country. In Johannesburg the sewerage and cleansing services both show a net revenue from fees, while 78 per cent of the expenditure of the building survey branch of the City



## NEW SOURCES OF LOCAL REVENUE

Engineer's Department is met by fees such as those charged for considering applications for approval under the bye-laws, and for the inspection of various kinds of buildings. The total income from these sources amounted to £1.7 millions.

We should assume that the policy under which the costs of sewerage and of cleansing are treated as services to be borne by the rates, without regard to individual benefit, is firmly established in this country. It has already been pointed out that the level of income likely to be derived from the most important local government services is largely determined by considerations of national policy. There are a considerable number of services performed by local authorities at the specific request, and for the convenience, of particular individuals and groups, and where the question of payment does not involve any major questions of policy. Such services might, in our view, derive an important contribution from payments towards their cost, and we suggest that this question might repay examination. But, in comparison with the total expenditure on local government services, the income likely to be derived will not make a marked difference to the main problem.

### FINES

Income from fines has never been of any importance to local authorities in Great Britain. Under the Justices of the Peace Act of 1949, all fines imposed by courts of summary jurisdiction are now paid to the Home Office. We would regard this change as right, and we do not think that local authorities should be interested in fines as a source of income.

### INCOME FROM PROPERTY

Among other miscellaneous sources of revenue may be mentioned income from local authority property. Apart from rents from municipal housing estates, where the disposal of any profits is governed by law, local authorities may receive rents from properties awaiting redevelopment, and some boroughs also own "corporate" property from which they derive an income.

### LICENCE FEES

In the case of licence fees, the Act of Parliament which empowers the local authorities to issue a particular licence may prescribe the fees to be charged; it may set a maximum limit; or it may allow local authorities to levy such fees as they see fit. In England and Wales the local taxation licences, consisting of dog, gun, and game licences, are levied

at a rate set by the central government but are administered and collected by counties and county boroughs. The yield of £1.2 millions in 1954-55 accrued to these authorities after the costs of collection had been met. Under the Finance Act of 1949, certain minor licence duties collected from hawkers, moneylenders and pawn-brokers, and licences to keep refreshment houses, were transferred from the Exchequer to the counties and county boroughs. Other matters for which local authorities are authorised to levy fees, are licensing petroleum stores (Petroleum (Consolidation) Act, 1928), race tracks (Betting and Lotteries Act, 1934), nurses' agencies (Nurses Act, 1943), theatrical employers (Theatrical Employers Registration Act, 1925), cinemas (Cinematograph Act, 1909), boxing and wrestling, and Sunday entertainments. In very few cases do the fees charged, which were usually fixed at the time the legislation was introduced, cover the costs of administration to-day.

In England and Wales, relatively few trades or businesses are subject to licence by local authorities. Trade licensing is far commoner in certain other countries. In Johannesburg, for example, there are over thirty different types of licence levied on traders and on places where a trade is carried on. Cobblers, ice-cream makers and fish-friers, laundries, places of public entertainment and Turkish baths are among those licensed by the city authorities. There are also licences for various types of vehicle, public vehicle licences, and poster advertisement licences. Many of the fees charged vary according to the size of the business. Many American cities also license a large number of businesses, and the revenues from these licences may be used for general purposes. Here too, the fee charged may depend on the type of business and the measurement of its activity.

There has, indeed, been an increasing tendency in the United States for business-licensing to be used as a taxing device, the fee payable often being based on the turnover of the business. Motor vehicle licences too, as in Great Britain, are charged at a fee rate which yields a substantial net revenue.

A clear distinction should, in our view, be drawn between licence fees charged where the licence is intended to be purely regulatory, and fees which are linked to licences but are charged to produce general revenue and are really excise duties. Fees for regulatory licences should not, in our view, be charged to exceed what is necessary to cover the costs of administration, but where the fee charged no longer meets this cost, local authorities, if they themselves prescribe the fee, might well consider raising it. Further reference to excise licences is made in Chapter X.

## NEW SOURCES OF LOCAL REVENUE

### PROFITS FROM TRADING ENTERPRISES

Most local authorities, other than county councils, run some types of trading enterprise: for example, water supply, passenger transport services, cemeteries, harbours, docks and piers, civic restaurants and markets. Prior to nationalisation, many local authorities also ran gas or electricity undertakings. Other examples of municipal enterprises run by local authorities are a municipal bank (Birmingham), a conditioning house and plant for dealing with the by-products of textile manufacturing (Bradford), a service for the collection and delivery of washing done in the municipal washhouse (Manchester), a bonded warehouse (York), and an oyster fishery (Colchester). These enterprises have accounts separate from those of rate fund services, and the transfer of profits in aid of rates is allowed under the Local Government Act of 1933. Although profits of £1.6 millions in 1953-54 were transferred from trading enterprises to rate funds by local authorities in England and Wales, some £7.5 millions was transferred from rates to meet trading deficits in the same year. In fact, markets were the one major trading service which showed a net surplus for local authorities in England and Wales as a whole. The aggregate net deficit in 1953-54 was £5.8 millions as against a net surplus of £6.1 millions in 1938-39. Local authorities have been faced with rapidly rising costs and resistance to increased charges, and this may account for the conversion of a net surplus into a net deficit over the last fifteen years.

Outside Great Britain, many local authorities run a much wider range of trading enterprise, and the profits are used for general purposes. In South Africa, for example, considerable sums of local revenue are obtained from trading profits. In many cases, these enterprises are of a competitive nature. Stockholm, for example, owns a company building houses and has shares in another owning its largest hotel. Norwegian municipalities own cinemas. Some Australian local authorities own hotels and others ice-manufacturing plants. Both Paris and Rome run municipal undertakers' businesses, and Rome also has a municipal zoo, central milk station, poster-publicity organisation and street hoardings. Some American cities run liquor stores. In South Africa, profits from the manufacture and sale of Kaffir beer by the municipalities are transferred to the Native Revenue Account and used for social purposes.

In Great Britain, apart from the public utilities, where, as we have seen, the few remaining services left to the local authorities do not at present yield a surplus in aid of rates, there remains the possibility



#### FEES, RENTS, RECOUPMENTS, ETC.

of the local authorities setting up trading enterprises in competition with private enterprise. Between 1919 and 1939, eight Bills seeking wider trading powers for local authorities were introduced into Parliament. In setting up such enterprises, a local authority may be seeking additional revenue or its primary object may be to provide a popular service. In either case the issue is highly controversial politically. We doubt whether any significant nett contribution to local revenues is likely to be obtained from this source.

## Chapter VII

### A LOCAL INCOME TAX

LOCAL income taxes are imposed in many countries overseas, notably in Norway, Sweden and Denmark and in a number of cities in several states of the United States. A surcharge is levied on to the cantonal income tax in Switzerland. We considered that the Swedish tax, which is a highly developed one, was the most suitable for detailed investigation on the spot. Accordingly we arranged for Mr. A. L. Imrie, City Chamberlain of Edinburgh, and Mr. L. S. Murphy, late H.M. Senior Principal Inspector of Taxes, to go to Sweden for this purpose. They brought back a wealth of material relating to the finance of local government there and to the relationship between local and national taxation. Their report, which we regard as particularly significant in relation to the subject of our study, is included as a Supplement to this Report. Its main features are summarised immediately below. References are quoted in parenthesis to the appropriate pages of the Swedish Report.

#### THE LOCAL INCOME TAX IN SWEDEN

The opening chapters of the Swedish Report describe very fully the Swedish system of public administration, the structure, functions and finance of local government, the income tax administration, both local and national, and the various sources of local revenue. There is an account of the main features of the local income and property tax and of such of the national taxes on income and capital as affect local finance and taxation. Public opinion in Sweden in relation to their taxation system was tested as far as was possible in a short visit, but no strong currents of opinion emerged. On the whole it seems to be accepted with as good a grace as any other system of direct taxation. Such informed criticism as exists is directed to the weight of direct taxation, and no substantial complaints about the design of the local income tax or about its administration were heard.

The first point that emerges is that there is a high degree of local independence and administration in Sweden through locally elected bodies. At the same time, the central government maintains some measure of control through the oversight of local decisions and

through the part taken in local administration by the officials of the provincial governor's office, who are state officials (p. 138).

A subordinate part is played in Swedish local government by taxes other than those on income and property (pp. 168-169). The property tax is in substance a tax on the income from property, and it does not need separate consideration.

Local and national income and property taxes are assessed and collected together by the same office and the same officials, leading to efficiency and economy in administration. Although there is a general similarity in scope between the Swedish and the United Kingdom national income and surtaxes, the Swedish system of collection on a preliminary assessment of income as it arises, with subsequent adjustments, differs fundamentally from the comprehensive system of deduction at the source prevalent in the United Kingdom. Moreover, there is a close link in Sweden between the right to vote and the obligation to pay taxes, and this is an important matter from the administrative point of view (pp. 156, 197-198). The differences in methods of administration and assessment as between Sweden and the United Kingdom are of great importance. This matter is discussed more fully on pages 81-83 below.

All local authorities, comprising cities, counties and primary communes, fix their own rates of local tax, and outside the six cities, which are themselves counties, the tax consists of two rates, one levied by the primary commune and one by the county council. The aggregate amount due is collected together with the national tax. The division between the local authorities is made by the *uppbordsverket* or tax charge office. In 1952 the rates of local income tax levied in the cities in Sweden ranged from 16.75 per cent down to 10 per cent. In rural communes the combined commune and county rate varied from 16.59 to 10.03 per cent. The average for the whole of Sweden was 12.75 per cent. There has been a remarkable degree of stability in the rates of tax from year to year, in contrast with the substantial rise in United Kingdom rate poundages in recent years. The local income tax is allowed as a deduction in computing the income on which the national tax is charged.

An analysis of the effect on taxpayers, on the local authorities and on the national exchequer of the system of allowing local tax as a deduction in computing income for assessment to national tax, is contained on pages 177-179 of the Swedish Report. The allowance of local tax as a deduction means that a proportion of local expenditure is indirectly borne by the national exchequer. The extent to which this occurs varies with the level of incomes in different local authority



areas; it is greater in areas where high incomes predominate than in areas where incomes are lower.

The comparative effect of evasion of local tax and of national tax is mentioned with particular regard to the possible concentration of evasion in a few areas. No positive information of the extent of evasion in Sweden was forthcoming. It is axiomatic that evasion of an income tax on some kinds of income is easier than evasion of a rate on land and buildings.

Another subject which is discussed in the Swedish Report is the problem of dividing up the profits of the many business concerns which operate in more than one local authority area. By reason of the differences in geography and of the greater localisation of industry, this problem is not so acute in Sweden as it would be in the United Kingdom. In the very small field in which splitting is necessary under the present United Kingdom law, e.g., in the case of branches in the United Kingdom of foreign companies, the problem is intractable and the results often unsatisfactory. Much thought would have to be given to devising the best solution if a system were proposed which involved such sub-divisions of the profits of many of the major concerns in this country.

There are substantial differences in incidence between a rating and an income tax system, and this is the subject of some illuminating comparative statements in the Appendices to the Swedish Report. Among individual taxpayers, the main changes of incidence would appear to be that householders would benefit as compared with non-householders, and that traders would benefit by comparison with employees. There would also be changes in incidence between ranges of incomes, and differences between residents in different areas.

The benefit to the trader arises from the fact that at present he pays rates both on his residence and on his business premises, while the wage and salary earner with a similar income and family circumstances is rated only on his residence. Under a local income tax, the trader would pay only the same amount as the wage- or salary-earner.

The change in incidence as between different income groups results from the fact that a local income tax on the Swedish system is proportional, although the proportional quality is modified if allowance is given for local tax in computing income for the progressive national tax. As against this, it is generally accepted that the British rating system is regressive. A tabular statement is given on page 230, but these figures are dependent upon the proper choice of the annual value of the residence normally occupied by persons in different income ranges, and there are no precise and up-to-date statistics on this subject.

## A LOCAL INCOME TAX

Since corporation profits are included in the Swedish local income tax, companies make a substantially larger contribution to local revenues than they would do under a rating system. There would be a corresponding change in incidence if a local income tax of the Swedish type were introduced in the United Kingdom. Concerning the change in incidence between different areas, there are reasons for thinking that the highly industrialised areas would come off best, but our investigators were not able to follow up this line of thought in any detail.

If, as in Sweden, local tax were deductible in computing income for the national tax, the Exchequer would, of course, lose tax in the case of those taxpayers (i.e., employees and rentiers) who at present get no deduction for local rates.

In summarising their views, Mr. Murphy and Mr. Imrie explain that, because of the fundamental difference in the structure of the income tax in the two countries arising out of the different approach adopted, they had been forced to the conclusion that a local income tax on the Swedish model could not be worked in the United Kingdom. In their view, the reasons which prompted the qualified acceptance by the Board of Inland Revenue in 1912 of the possibility of superimposing a local income tax on the state tax administration<sup>1</sup> are no longer valid. As an alternative, they suggest that it might be possible for local income tax administrations to be set up which would employ the same basic information as the national system and yet work independently towards a separate assessment and payment. There would have to be machinery for putting the relevant information from national returns at the disposal of local authorities, and it would probably be necessary to set up a national body charged with the duty of apportioning the profits of industry and commerce. The administrative difficulties are formidable, but they thought this approach more promising than an attempt to copy the Swedish system.

## A LOCAL INCOME TAX IN GREAT BRITAIN

The major differences between Sweden and the United Kingdom in the methods of administration and the basis of assessment, to which reference is made in the Report by Mr. Murphy and Mr. Imrie, flow from fundamental differences in the design of the two tax systems, having their origins no doubt in the different historical development

<sup>1</sup> The Board's views were given in a memorandum laid before the Departmental Committee on Local Taxation, 1912-14 (Chairman: Sir John Kempe, KCB), Cmd. 7315-6, 1914. The memorandum is reprinted on pages 236-241 of this report.



of the two nations and in certain basic differences in the methods of government, such as the reliance by the Swedish authorities on a national system of personal registration. The Swedish tax system is entirely personal in character, resting primarily on the annual personal return of income. The computation of profit or income is undertaken by one office, and the results are then handed over to another office for the actual assessment and collection of both the national tax and the local tax.

By comparison, the United Kingdom system has never entirely lost that element of anonymity which was so important in securing the passage of the original Income Tax Act, and it is still based primarily on the source of income, with little regard to the individual or individuals to whom it goes. Thus, in the case of landed property, the tax was—and still is—charged on the full annual value, although that annual value may be enjoyed partly by the occupier, partly by a mortgagee and partly by a lessor or ground landlord. The tax on interest is charged on the payer, who recovers it from the payee, and dividends are charged with tax as part of the profits of the company. Originally, of course, the British tax was levied at a flat rate, and little regard was paid to the personal circumstances of the recipient of the income. One might have thought that the introduction of graduation, together with the reliefs and allowances designed to reflect differences in personal circumstances, would have converted the tax from a tax on income as such to a tax on individuals, and that the administration would have gradually altered correspondingly. This, indeed, might well have happened but for the introduction of "Pay As You Earn" and the administrative problems to which it gave rise. Under the PAYE system, the tax is collected through the employer with no regard to the place of residence of the employee, and in the great majority of cases no assessment at all is now made. Indeed, the position as it has now developed is that there are effectively only two groups of people of whom it can be said that assessment and collection of tax on an individual basis are the normal rule. These are individuals and partnerships assessed under Schedule D, and surtax payers. For the rest of the population, tax is collected for the most part at source under PAYE or by deduction at source in the case of dividends, interest, etc. The PAYE basis is sufficiently accurate for an annual assessment to be dispensed with for all the lower ranges of income. Even for those incomes lying between the top of the reduced rate band and the starting point of surtax liability, the tax administration has normally no interest in computing either the total income or in making an assessment. Any earnings will have been dealt with under



PAYE, and for the most part any unearned income will have suffered deduction at source at the full standard rate, or will have been taken care of by an adjustment of the PAYE code.

The PAYE records are arranged by reference to the employer, and there is no means whatever, other than sorting through them individually, to relate them to place of residence. Even then the residence is not known in many instances, the records merely showing the employer's name and address and the employee's department and works number. For the vast majority of the income-earning population, therefore, the Inland Revenue knows neither their place of residence nor their total income. The Swedish system involves an annual assessment of the total income of every person, and it is a matter of no difficulty to make an assessment to the local or communal income tax at the rate in force where the taxpayer resides, and to collect it along with the national tax.

For these reasons, we accepted the view expressed by Mr. Murphy and Mr. Imrie that it would not be possible to impose a local income tax here on the same lines as in Sweden. We therefore proceeded to consider, as they suggested, whether it would not be possible to devise a local income tax which would stand on its own feet with a separate local administration independent, or largely independent, of the national administration. For the reasons given on pages 85 and 91 below this does not mean that work would be duplicated all along the line. Nevertheless, if an attempt were made to impose a local income tax on lines as complicated as that of the national tax, it would undoubtedly place an enormous burden of work on local authorities. The clear and obvious answer to this is that if a local tax were to be imposed, it would have to be much simpler than the national income tax is in this country. We appreciate that, in their *Second Interim Report*, the Royal Commission on the Taxation of Profits and Income considered various forms of simple income tax at the national level and rejected them. Their reasons for so doing are not, in our opinion, relevant to the question whether a simple income tax would not be appropriate for the use of local authorities. The Royal Commission were considering a simple tax as a substitute for the income tax for the lower income ranges only (e.g., up to £500 a year), the existing income tax being retained for incomes above that level. Their objections to a simple tax amounted, briefly, to saying that a simple tax must necessarily be very rough and ready as compared with the type of income tax we know, and that people would object strongly to it, firstly because the anomalies would be serious as compared with the income tax it replaced, and secondly because, as the simple tax would apply to the

lower income groups, it would be the poor people who would be said to suffer as a result of any such anomalies. In other words, the argument would be put forward of "one law for the rich and another for the poor." A local income tax, however, would replace revenue which, if it were to be raised locally, could only be raised under the present system by the rates. The rates are generally agreed to be regressive, and a local income tax, however simple, is at least proportional to income and must represent an improvement in incidence. We are, moreover, thinking in terms of a local income tax which would be levied at rates of about 1d. to 3d. in the £. This is far lower than anything which could be contemplated for national purposes, and any anomalies which might exist would be trivial. In the light of these considerations, it would be difficult to condemn the tax on the grounds advanced by the Royal Commission.

#### A SIMPLIFIED LOCAL INCOME TAX—WAGES AND SALARIES

In terms of total amount, wages and salaries represent by far and away the most important item of income. Moreover, because of the numbers of people involved, the taxation of wages and salaries accounts for the greater part of the administrative burden. The first essential of a simple local income tax is that it should provide an easy and straightforward way of dealing with wages and salaries. The obvious step would be to collect the tax, at 3d. in the £ or whatever rate was chosen, from the employer, the tax being charged on the total amount of the payroll. The employer would be entitled to deduct the tax on paying the wages or salaries. The essence of this proposal is that there should be a single computation of the tax, namely on the total amount of the payroll, and that the tax should be paid over by one person, namely the employer. The tax would in this respect be similar to the payroll taxes which have been imposed successfully in a number of cities in the United States.

The tax would, in effect, be "non-cumulative" and would be charged on "gross pay" with no reliefs or allowances and no deductions for tools, clothing, insurance premiums, etc. For the reasons already explained, these features cannot be regarded as a substantial objection if the tax is compared with the rates.

No assessments would be made, or needed, on individual employees, and there would be nothing corresponding to the PAYE coding procedure. In order to deal with domestic and other part-time workers, it might be desirable to omit from the "payroll" anyone earning less than £2 a week.

Some multiple concerns pay their employees from a central point.

## A LOCAL INCOME TAX

They would have to divide up their payroll according to the areas in which their employees worked. For most concerns affected this would be a straightforward job, and we do not feel that it would be unreasonable to expect employers to keep their records in a way which would enable the necessary information to be furnished.

The tax would be collected from the employer monthly, quarterly or at whatever other intervals might be thought convenient.

It would be necessary to place an obligation on employers to notify the local authority concerned, and to make returns and pay the tax. The task of the local authority would be limited to ensuring compliance with these provisions. This would not involve an undue administrative burden. Normally there would be no contact with the individual employee.

A tax of this kind imposed on the payroll would accrue to the local authority in whose area the taxpayer worked. This represents an important change in incidence, and a different pattern of yield would result in comparison with the rates, where the yield accrues to the local authority area where the taxpayer lives. The point is discussed in detail on pages 93-94 below.

### EXTENSION OF THE TAX TO THE SELF-EMPLOYED

It would not be acceptable in this country to impose a tax on wages and salaries and let profits go untaxed—even with a rate as low as a penny or two in the £. It would therefore be essential to extend the tax to individuals and partners engaged in business or in the professions. Indeed, many of the cities which have imposed payroll taxes in the United States have imposed some compensating tax on business profits. The extension of the tax in this way to business profits and professional incomes does not mean that the local authority would be faced with the task of computing business profits. On this point, again, Swedish experience is valuable. In Sweden, the computation of profits is undertaken by one office, and the results then handed over to another office for the actual assessment and collection of both the national tax and the local tax. There is no reason why, in this country, the computation of the profits should not, by law, be handled by the Inland Revenue, and the result notified to the appropriate local authority for assessment and collection of the local tax. This proposal would eliminate the risk, otherwise a real one, that the two taxing authorities would take divergent views on the same problem. It would be essential for strict provision to be made that the staff of the local authority dealing with this work should be bound by the same conditions of secrecy as apply to the income tax.



## NEW SOURCES OF LOCAL REVENUE

### COMPANY PROFITS

In principle, a local income tax ought obviously to extend to companies as well as to individuals in trade. The computation of the profits and the assessment of the tax would follow the same lines as suggested above for individuals and partnerships. This would give rise to no great difficulty. The problems arise, however, when one comes to determine the local authority area which would be entitled to levy the tax. Most companies have their works and offices as well as their registered office—which constitutes their legal place of residence—in a single area, and this would be the area entitled to tax the profits. There is no difficulty here. But many companies operate in more than one local authority area, and there would be considerable difficulty in dividing up profits between the areas in which they operate. Some companies have their legal residence in one area, but operate largely elsewhere. Banks, insurance companies and financial institutions would give rise to particular difficulties. There are also companies which are registered in the United Kingdom but operate overseas, and shipping and air transport companies. For these reasons, the taxation of company profits would present greater problems here than in a country like Sweden, where industrial and commercial development has not proceeded to the same extent.

We greatly doubt whether any body of rules could be drawn up which would provide in an acceptable manner for the determination of the local area of taxation in all special types of case to which we have referred. But we do wish to stress that all that is really at stake is the taxation of company undistributed profits. If companies as such were excluded from the tax, dividends and interest received by individuals would still be charged in their hands. If the matter is looked at in this light, the exclusion of companies is a much less serious matter than would at first sight appear.

While we appreciate that arguments can be advanced in favour of taxing company undistributed profits, our own view is that the practical problems are such that they would have to be excluded. The tax would thus become a personal income tax.

If, however, it were felt that company undistributed profits must be taxed, this could be done by a system of central assessment and payment into a municipal fund for subsequent division among local authorities. Alternatively, some compensating charge could be levied on companies, e.g., an additional rate poundage or, if the local income tax were introduced concurrently with the abolition of derating, it might be felt that this was a sufficient additional burden on companies.

If companies were exempted, the exemption ought to be confined,

## A LOCAL INCOME TAX

substantially, to public companies. It should not be left open to the small business man to contract out of the tax by turning himself into a company.

### ALLOCATION OF PROFITS AMONG DIFFERENT AREAS

Whether companies were brought under charge or not, it would be necessary to have some rule for allocating profits where a business operated in more than one local taxing authority area. To some extent this problem would be eased by a judicious choice of type of local authority empowered to levy a local income tax. This point is dealt with on pages 92-93 below. But there would still remain many concerns which would overlap any boundaries which might be chosen. Some way would have to be found of dividing up their profits as between the different areas in which they operated. The relevant text in Sweden is quoted in Mr. Murphy's and Mr. Imrie's report. It is couched in very general terms; it seems to work well enough with the aid of a Central Office in Stockholm, but the problem in Sweden is much simpler than in this country as industry and trade are much more localised, and the big industrial areas found in this country around cities such as London, Birmingham and Manchester have no counterpart in Sweden. In this country, it would be essential to have some clear and unambiguous rule laid down by Act of Parliament. This could only be a rule of thumb, but we believe that such a rule could be found which would be generally acceptable. It must be borne in mind that if local authorities were empowered to levy a local income tax, there would probably be few areas where such a tax was not imposed, and the spread of rates would probably be small. From the point of view of the taxpayer, therefore, the basis of division of the profit might not be of any great moment; it would be the local authorities who would be the parties most concerned.

Three possible factors by reference to which profits might be allocated are:

- (i) Rateable value;
- (ii) Turnover;
- (iii) Payroll.

"Rateable value" was the basis suggested by Viscount St. Aldwyn, formerly Sir Michael Hicks-Beach and Chancellor of the Exchequer, and this suggestion was considered by the 1912-14 Departmental Committee on Local Taxation, to which we have already referred on page 81. There are serious objections to it, principally that rateable

value has little correspondence with profit, which is what we are really trying to ascertain. There is little to choose as between the other two, except that the "payroll" basis would avoid the difficulty, which would arise under the "turnover" basis, that a notional turnover would have to be determined where goods were transferred from one department of a business to another and the departments were in different local taxing areas. In some cities in the United States, a formula is adopted which is based on both payroll and turnover.

It might be desirable, following the Swedish example, to deal with cases of this kind through a special central office which would allocate profits and might indeed undertake the whole job of assessment and collection, remitting the proceeds to the appropriate authorities.

The problem of the allocation of profits would be of minor importance if companies as such were excluded. But it would be a major issue, both from the legislative and the administrative point of view, if companies were brought under charge.

#### INVESTMENT INCOME

We have dealt with wages and salaries and with business profits. The most important remaining item is investment income. It would be impossible to ignore this: in every community there are individuals with large unearned incomes, and to allow them to go untaxed—particularly when they would benefit from any reduction in the rates which the introduction of a local income tax might enable to be made—would be indefensible. The only real solution would seem to be to require all persons with an investment income exceeding, say, £100 to render a return to the local authority and pay the tax. This would not, perhaps, present any very great difficulty; with an exemption limit of the kind suggested, the number of people in any particular local taxing area would be comparatively small; the return, being limited to investment income, would in most cases be simple and the assessment straightforward. For surtax payers, where problems often do arise, co-ordination with the surtax authorities, on similar lines to that suggested for business profits, would provide a ready answer.

As rates would continue to be levied, there might be thought to be a case for exempting the income from houses and other real property (Schedule A) from the local income tax. Administratively this would be a further simplification, but we have some doubts as to the logic of such a claim. So far as the owner occupier is concerned, in most cases the £100 exemption for investment income would cover him even if there were no specific exemption for Schedule A income.

There may be some criticism of the proposed exemption limit on



## A LOCAL INCOME TAX

the ground that the person with a salary of £500 would pay on the whole, while a person with £400 salary plus £100 investment income would pay on £400 only. Broadly speaking, however, the £100 does no more than correspond to the £2 per week exemption suggested for the payroll tax. This is really only a debating point: the maximum amount at stake would only be £1 or so and it is not possible to base much of a grievance on this. It would, however, be important to make the exemption limit a true exemption limit and not an allowance—i.e., the person with £200 investment income would pay on the full £200 and not on £100 only (viz., £200 less £100).

The exemption limit could be fixed at a lower figure than that suggested. This would mitigate any feeling of resentment on the part of other taxpayers, but we should not be in favour of reducing this figure too much. To do so would greatly increase the field of direct assessment, and if the figure were pitched too low, it would be widely ignored.

If companies as such were exempted, dividends would be assessed on the shareholder in the same way as any other investment income. If, however, companies were charged to tax, the assessment would be on the total profit, and the part subsequently paid out in dividend would already have borne tax so there would be no case for assessing it again in the hands of the shareholder. Administratively this would simplify the position so far as the shareholder was concerned, and it would mean that tax would be collected from all company dividends, irrespective of amount. The tax, however, would go to the authority for the area in which the company operated, and not to the authority for the area in which the shareholder lived. Many people would regard this as wrong. The point is discussed at greater length on pages 93-94 below.

## OTHER INCOME

There are a number of other miscellaneous items of income not so far dealt with. Of these, old age pensions, widows' pensions, sickness and unemployment pay, disability pensions and other social security benefits and family allowances might well be exempted—partly on sentimental grounds but also for the solid reason that if no allowance is to be given for the National Insurance contributions, it would be wrong to charge the benefits. Similarly, as no deduction would be given for children, the family allowance should not be charged to tax.

Private pensions (i.e., from an employer) would be charged to the payroll tax in just the same way as for income tax purposes they now come within the PAYE system.

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Where an individual has minor sources of earned income outside the scope of the payroll tax (e.g., earnings from writing or broadcasting fees) these might be dealt with in the same way as investment income: if the total exceeded £100 there would have to be a return made to the local authority and direct assessment. The £100 exemption would apply to the total income not already charged: thus if the miscellaneous income *plus* investment income exceeded £100, a return would have to be made.

## SPECIAL GROUPS OF EMPLOYEES

Certain special groups of employees, notably the armed forces and merchant seamen, would present a particular problem, but we have no doubt that some solution could be found, although it would have to be on rough and ready lines.

## CHARGES ON INCOME

Charges on income are essentially negative investment income and an allowance should be given only against investment income. This would mean that charges can be ignored except in those cases which would be brought under direct assessment anyway.

This proposal would mean that where, as sometimes happens, the charges exceed the amount of the investment income, no allowance would be given for the excess against other income. The commonest case of this kind is where mortgage interest paid to a building society or other body exceeds the net Schedule A assessment. This situation arises because the mortgage, and consequently the interest on it, relates to a post-war value, while the Schedule A assessment is determined by reference to pre-war value. The problem is probably a temporary one, but in any event we do not think that there is much equity in a claim that relief should be given for the excess interest paid.

## FORM OF THE TAX

In the exposition in the preceding paragraphs, we have approached this matter from the point of view of the individual sources of income. This, indeed, follows the legal framework on which the income tax in this country is constructed. In doing this we have accounted for all the items that go to make up an individual's total income, as the following summary shows:

- (a) Wages and salaries would come under the payroll section of the tax.

#### A LOCAL INCOME TAX

- (b) Business profits and professional earnings would be charged by direct assessment.
- (c) Dividends and interest from companies would be charged by direct assessment if our proposal to exclude companies as such is accepted; if not, they would be charged as part of the company's profits following the present (national) income tax practice.
- (d) Other investment income and Schedule A income would be charged by direct assessment (subject to the £100 exemption).
- (e) Pensions from an employer would be charged under the payroll tax. Social security benefits would be specifically exempted.
- (f) Minor sources of earned income would be dealt with by direct assessment (subject to the £100 exemption).

#### YIELD

At the current levels of income, a local income tax confined to personal income would yield about £50 millions per penny of rate charged, if it were levied by all local authorities. Thus a 3d. rate of tax would produce an aggregate yield of about £150 millions. The yield from undistributed profits if they were brought within the charge might be put in round terms at £25 millions with a 3d. rate of tax, but the figure would obviously depend on the line taken on numerous points of difficulty.

There is, in our view, no reason why, in the case of individuals, local income tax should be allowed as a deduction in computing the national tax, and no adjustment has been made on this account in computing the yield of tax. The yield from company undistributed profits is also given gross but here the argument in favour of allowing a deduction in computing the national income tax and profits tax is much stronger; if this point was conceded it would reduce the yield from undistributed profits to about £14 millions (with a 3d. rate of tax).

#### ADMINISTRATION

Provided co-operation with the Inland Revenue on the lines suggested could be secured, the administration of the local income tax on the basis described should not present any undue difficulty for local authorities. The most troublesome part would undoubtedly be the direct assessment of people with investment incomes; here the help which could be obtained from the Inland Revenue would probably be limited to surtax payers. But the difficulties must not be exag-



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gerated. The local authority is already in touch with most of these people through the rating system and, with people below the surtax limit, the potential loss of tax would not, in any event, be very great.

### AUTHORITIES EMPOWERED TO LEVY THE TAX

Determining what authorities could levy the tax is a decision of the first importance. It seems to us that an important local government function like the raising of money, should be in the hands of an elective body. It also seems to us that this body should be as local as is consistent with the efficient discharge of the function, since public interest in local government can most effectively be maintained if the organisation allows a ready contact between those who levy and those who pay. This contact is secured under the present rating system by the fact that the responsibility for levying rates rests with county borough councils and county district councils, and in searching for new sources of revenue we are seeking to strengthen the link of local responsibility.

Nevertheless, while we have expressed the view that the administrative operation of an income tax for local government purposes is feasible with some measure of assistance from the established machinery of the central government, we think that the operation would require the kind of administrative organisation which goes with substantial resources. We contemplate that the tax should be levied at the county/county borough level although we appreciate that the division between counties and county boroughs would not provide the most effective solution for the problems of splitting profits and of incidence, to the latter of which we refer below. We do not think that this problem of machinery presents any bar to the adoption of a local income tax, but we think that the choice of the most effective unit is closely bound up with the question of the units selected for the performance of other local government functions.

We understand that the question of local government reorganisation is under consideration, and we recommend that if our recommendation for a local income tax is accepted, the choice of a unit for its administration should be taken into account in connection with this reorganisation.

### LEGISLATION

The legislation would have to prescribe in detail the persons and income chargeable, and to provide for the assessment and collection of the tax and the confidentiality of the records. It would also have to determine what authorities could levy the tax, and to lay down

## A LOCAL INCOME TAX

maximum rates. It would be left to the local authorities concerned to determine whether they wished to levy the tax and, if so, at what rate.

### INCIDENCE

So far as the incidence of the tax on the individual is concerned, there is little we would wish to add to the points made by Mr. Murphy and Mr. Imrie in their report, the relevant part of which is summarised at the beginning of this chapter.

### AREA OF ACCRUAL OF REVENUE

The distribution of the yield of the tax as between local authorities would differ considerably as compared with the rates. A local income tax of the kind we have described proceeds very largely on the basis of the place of work or business—i.e., the point of origin of the income. The rating system proceeds primarily on the basis of the place of residence of the ratepayer—although it can well be argued that the rating of business premises is really taxation based on the place of origin of the income. The essential point at issue is whether local authorities should be entitled to levy taxes on income arising in their area, even though the person enjoying that income resides elsewhere. A similar problem arises as between different countries in the field of national taxation, and it is of course the opposing views taken by different countries which give rise to the problems of double taxation. For what the point is worth, the arrangements made both in this country and elsewhere for the relief of double taxation recognise that normally it is place of origin which has the prior right of taxation, not the place of residence. Whatever may be the rights or wrongs of this theoretical issue, there are two points we would like to make. Firstly, it is worth serious consideration whether a local authority revenue system under which part of the revenue is derived from a tax based on origin and part from a tax based on residence, would not be better founded than one based on residence only. Secondly, over the greater part of the field, place of origin and place of residence are synonymous. Most businesses would still be taxed in much the same area as at present, for in general terms their profits arise where their business premises are situated. Most people live in the same area as they work. Although in some places the problem will be of some magnitude, its importance for the country as a whole should not be exaggerated. If, for example, the tax were levied only at the county/county borough level, this would minimise the changes in distribution of revenue as between the various local authorities. In the last resort the matter can always be dealt with by adjustment of the Exchequer

Grant. We have already pointed out earlier in our enquiry that a change in the local tax system will in any event require a complete review of the grants system.

Our own view is that a local authority ought to be entitled, if it so wishes, to levy taxes on the wealth created in the area it represents, and that it ought not to be debarred from so doing by the fact that the owner of the income is resident elsewhere. In other words, we regard the local authority as standing *vis à vis* its own area in much the same position as the central government stands *vis à vis* the country as a whole. And no one would now argue as a general principle that the state ought not to tax income arising in the United Kingdom because the owner of the income is not resident in this country. We recognise that many of the services for which a local authority is responsible are particularly directed to the residents of its own area, and while we uphold the right in principle for local authorities to tax income arising in their own area, we do not think it would be right to transfer the whole burden of local expenditure on to a tax based on income arising, as distinct from on residence. In other words, we favour a judicious mixture of the two.

#### CONCLUSIONS

We believe that a local income tax could be operated equitably and successfully, provided the tax were confined to personal incomes and provided it were imposed at a maximum rate not exceeding, say, 3d. in the £. Even at this modest level, it would prove an exceedingly valuable additional source of revenue for local authorities, producing a yield for the country as a whole of about £150 millions.

If, on grounds of equity, it were felt essential that company undistributed profits should be brought under charge, there are a number of special devices which could be adopted to do this or to obtain an equivalent contribution from companies. For example, the tax could be assessed centrally and paid into a municipal fund for distribution among the local authorities. Alternatively, local authorities imposing the local income tax could be given powers to impose an additional rate poundage on companies to compensate for their exemption from the local income tax.

Finally, we would make the point that the finances of local authorities cannot be regarded as isolated from the national finances, and if the imposition of a local income tax confined to individuals produced a distribution of tax burden unduly favourable to companies, it is open to the central government to take this factor into account in deciding its own tax policy.



## Chapter VIII

### A LOCAL ENTERTAINMENTS TAX

SINCE its inception in 1916, the Entertainments Duty imposed in Great Britain has been a central government tax. Its terms and rates are laid down by statute and it is administered and collected by the thirty-two Collection Areas of H.M. Customs and Excise in Great Britain. The duty has thus always been administered by the central government and its yield directed to the Exchequer. In 1954-55 the yield was £41 millions, equal to about 17/- per head of the population. 86 per cent of the yield came from the duty on cinemas (levied at the highest of the three scales of duty), 7 per cent from football and racing (the middle scale), 5 per cent from theatres and music halls (the lowest scale), and 2 per cent from other sports and entertainments.

Only in New Zealand of the twelve countries whose revenue systems have been surveyed is the entertainments duty levied exclusively by and for the national or federal governments. There is in fact a great variety of practice:

- (i) In South Africa, the duties are levied exclusively by the provincial governments.
- (ii) In Australia, they are levied by the State Governments, except New South Wales and Queensland.
- (iii) In Canada, they are levied by the provinces, and by some local authorities in Saskatchewan, Newfoundland and Quebec. In Quebec local authorities must share the yield of the tax with the province.
- (iv) In the U.S.A., entertainment taxes are levied by the federal government and by forty-four of the forty-eight state governments, as well as by local authorities in seventeen states (197 with a population exceeding 10,000 in 1955).
- (v) In Switzerland, they are levied by the cantons and by some communes (in 1952 by thirty-seven of the seventy-one communes with a population exceeding 7,000). Some other communes receive a share of the cantonal tax.
- (vi) In Denmark and Sweden, local authorities receive a share of

## NEW SOURCES OF LOCAL REVENUE

the central government duty, and in Sweden they administer and collect it.

- (vii) In Western Germany, entertainments taxes are levied exclusively by and for the local authorities, but the rates of tax are generally set out in provincial legislation.
- (viii) In Norway, both the central government and the local authorities levy entertainments taxes.
- (ix) In France and the Netherlands, the taxes are exclusively local. In France, the central government sets limits to the rates of tax which the local authorities may levy.

It is evident that entertainments duties are levied as often by local as by central government authorities.

We decided therefore to investigate the operation of local entertainments taxes in other countries, and our Secretary, Mrs. E. B. Wistrich, visited the Netherlands and Western Germany (*Land North-Rhine Westphalia*) for this purpose. A summary of this investigation is given below.

### THE LOCAL ENTERTAINMENTS TAX IN THE NETHERLANDS

An entertainments tax was first imposed in the Netherlands in 1809, but since 1851 such taxes have been levied exclusively by the municipalities. To-day 885 of the 1,010 municipalities containing 98 per cent of the total Dutch population impose a local entertainments tax. Municipal revenues are at present very largely derived from central government grants and the Municipal Fund, and the amount of local in relation to total taxation has progressively declined to 3 per cent of total taxation in 1953. Local entertainments taxes remain one of the few purely local taxes levied, administered and collected by the municipalities.

Under the Municipal Law of 1851, which sets out the powers and functions of local authorities, a number of taxes which all municipalities may levy are enumerated, and among these is a tax on "theatrical performances and other entertainments." This is the only specific statutory provision governing the tax; the municipalities are in law free to decide whether to levy an entertainments tax, and to frame bye-laws prescribing the entertainments to be chargeable to tax and those exempt, the rates of tax, and the methods of administration, collection and inspection. Dutch law, however, prescribes that all municipal bye-laws relating to taxation must be scrutinised and approved by the Crown. The draft bye-laws introducing or modifying the forms of the tax are therefore submitted to the Ministry of the Interior whose officials scrutinise them to see if they conflict with any

articles of the Constitution or with any national law. Approval has never been withheld in the case of an entertainments tax bye-law, and the chief concern of the Ministry is to ensure that the local bye-laws regulating the tax are within the bounds of law and jurisprudence. Where, for example, a bye-law proposes to tax a function which the High Court has ruled is not an entertainment, the Ministry will advise the municipality in question to revise its bye-law accordingly. But the Crown may not in law direct the municipalities to include certain provisions in their bye-laws; the control is a purely negative one. In fact, there is a very wide variation in the content of municipal entertainments tax bye-laws, particularly regarding the entertainments which may be accorded relief from tax.

The discretion of the municipalities to decide the amount of tax to be levied is exercised within the system of financial tutelage under which they operate. Firstly, municipal budgets are subject annually to ratification by the provincial authorities. Secondly, all taxation bye-laws, including bye-laws proposing a change in the rate of tax to be levied, must be approved by the Crown, and in this matter the Crown takes the advice of the provincial authorities. This machinery of supervision over financial affairs enables the higher authorities to exert pressure on the municipalities as they fix their rates of tax. Furthermore, an overwhelming proportion of total local government revenues is derived from grants from the Municipal Fund and specific grants made by the central government.

In recent years the central government has brought pressure to bear on the municipalities to introduce entertainments taxes where they were not already imposed, and to levy certain minimum rates of tax. Under the Finance Act of 1948, municipalities were threatened with reduced grants from the Municipal Fund if they did not use their own taxes to the fullest extent. The Act stipulated that minimum rates of 35 per cent should be levied on admission to cinemas and 20 per cent on other entertainments. The sanctions contained in the Act were never actually used, and the provision in question was repealed in 1952, but, combined with pressure exerted through the indirect controls outlined above, it did have the effect of causing a general rise in entertainments tax rates, and the introduction of a number of entertainments taxes in municipalities which did not impose them before. These influences are essentially the result of the present weak financial position of the municipalities which makes them dependent on the central government for revenues; their legal autonomy to frame their own bye-laws governing the tax within the limits described above remains.



The sole statutory definition of taxable entertainments is "theatrical performances and other entertainments." This definition has been interpreted and elaborated by a series of High Court decisions in individual cases. In general, any entertainment where the people admitted or participating can be said to be seeking entertainment is held to be taxable. Included are entertainments where the public are spectators, such as a cinema or theatre shows; entertainments where the public participate actively, such as a dance or whist-drive; and entertainments where there is no charge for admission such as fairs, bazaars or sports displays. Scientific lectures, religious and political meetings, swimming pools and skating rinks are held not to be taxable entertainments.

The bye-laws relating to the entertainments tax vary from municipality to municipality, but the usual practice is for all entertainments to be taxable, with certain specific exemptions. No general description of these exemptions can be given, except to say that the larger municipalities tend to allow more exemptions than the smaller ones, and that far fewer exemptions are allowed in comparison with the exemptions from the entertainments duty in Great Britain. Some municipalities have powers under their bye-laws to grant relief to certain entertainments at their discretion.

A certain consistency is maintained in the interpretation of municipal bye-laws through the system of appeal. Any citizen who is dissatisfied with the municipality's decision that an entertainment is taxable under a bye-law, or that it does not qualify for exemption, may appeal against the Municipal Council's decision to one of the fifteen special administrative courts which deal with all taxation matters, and a final appeal lies to the High Court. The decisions given ensure, for example, that a touring entertainment is not taxed in one municipality and exempted in another where the relevant provisions in the bye-laws of both municipalities are the same. Although the appeal procedure is simple and inexpensive, few appeals are now made. Most questionable points have been settled over the long period that the tax has been in existence and there is established case law on the subject.

Where a charge for admission to an entertainment is made, the method of imposing the tax is nearly always by levying a percentage rate on the price of the tickets of admission. There is no progression in the tax rates according to the price of admission. The method used is to levy the tax on the inclusive price, i.e., the price plus the tax, but in such a way as to avoid taxing the tax itself. For example, a rate of 25 per cent is levied as 20 per cent but charged on the inclusive

price.<sup>1</sup> In certain cases, and particularly where there is no charge for admission, the tax may be levied on the area of the ground used or the number of seats in the building, or a fixed charge per day may be made, but these types of levy account for only 10 per cent of the total tax yield.

A survey of rates levied in 1953 by seventy-one municipalities with populations ranging from 900 to 859,000 shows that nearly all levied rates of 20 per cent on admission to theatres, concerts, sporting events and exhibitions, and between 20 and 50 per cent on other types of entertainment. Some municipalities levy different rates of tax for the same entertainment, depending on whether the entertainment is presented by a professional or non-professional organisation, or the use to which the profits from it are put. In the case of cinemas, most municipalities levied a rate of 35 per cent on the majority of film shows, comprising feature films accompanied by a Dutch newsreel or a short cultural film. Many municipalities, however, levied much lower rates on Dutch feature films and on films held by the Board of Censors to be "cultural," and higher rates on film shows where there was no Dutch newsreel. Rates of tax do not appear to vary substantially with the size of the municipality.

There has, however, been a considerable variation in the general level of tax rates since 1945. Up to 1946, 20 per cent was the usual maximum rate levied on film performances, and lower rates on other types of entertainment. In the post-war period, there was pressure from the central government to levy higher rates and this resulted in a general increase of the rates on film performances (see page 97). Following a recent enquiry by the central government into cinema revenues, the central government in 1954 revoked its previous advice to the municipalities to levy the higher rates, and rates on film shows are now gradually being reduced to between 20 and 25 per cent.

Administration, collection and inspection of the tax do not present any serious problems. The only contentious work concerns decisions whether an entertainment is taxable or exempt under the bye-laws. Such decisions are generally taken by the Director of Taxes (an official) or his subordinate, but in the smaller municipalities with a population of under 20,000, they may fall to the Burgomaster and Executive Council. In either instance an appeal lies to the Municipal Council. In The Hague inspection is strict and penalties for non-payment of tax are severe. Administration tends to be less exacting in small municipalities. Although it is not possible to calculate the

<sup>1</sup> Thus with a 25 per cent rate of tax a net admission price of 4s. (to use sterling figures) would attract duty of 1s., making an admission price of 5s. The tax in fact is levied on the 5s., but the rate is abated to 20 per cent to restrict the tax charged to the correct figure of 1s.

precise costs of administration, an estimate made for The Hague suggests that it is not greater than 3 per cent of the total tax yield.

The tax is widely accepted in the Netherlands as an old established local tax and there seems to be little concern about variations in rates of tax which are reflected in admission prices, or about differences in the provisions of the bye-laws. The number of exemptions allowed is generally small and most concern entertainments likely to be promoted by purely local organisations not professionally engaged in providing entertainments. So far as the professional promoter is concerned, the exemptions are of relatively small importance. Consequently few promoters are faced with varying exemptions as their entertainments tour from one municipality to another. Certainly the possibility of easy and inexpensive appeals keeps local interpretation of the bye-laws consistent. Dissatisfaction with the tax on the part of the promoters is centred on the overall level of the tax rates rather than on variation in rates. For example, the cinema distributors' organisation recently threatened a "strike" in protest against high rates of tax, and following an enquiry, the Government recommended to municipalities a reduction of rates on film shows to between 20 and 25 per cent. A recently formed organisation of amateur cultural societies is also working for a general reduction in tax rates on certain types of entertainment.

#### THE ENTERTAINMENTS TAX IN WESTERN GERMANY

Local entertainments taxes were imposed in Germany before 1914. Between 1921 and 1933, regulations introduced an increasing degree of uniformity in the tax provisions, and from 1933 to 1945 there were standard tax provisions for all municipalities. Under the new federal Constitution, the tax falls within the jurisdiction of the provinces (*Länder*) and each province to-day has its own entertainments tax law which establishes what entertainments the municipalities may tax, what exemptions they may allow, and methods of administration. It is also the general practice to set out the rates of tax to be levied. The municipalities (including city-counties) administer the tax and receive the yield. Counties do not usually levy the tax themselves, but they may precept on the municipalities for a share of it.

In *North-Rhine Westphalia*, the municipalities possess a certain closely limited discretion under the law to frame regulations relating to the administration of the tax, subject to approval by a higher authority. They may also decide whether an entertainment qualifies for exemption or a reduction in the rate of tax according to the law. Appeals against local decisions are not heard by the *Land* Ministry but



by an administrative court, or, in the final instance, by the Higher Administrative Court of the *Land*. But where an entertainment is to be promoted in more than one municipality and the exemption or reduction depends on an assessment of its cultural or educational value or artistic standard, the decision is taken by the *Land* Minister of the Interior, after consultation with the Ministers of Finance and Education, and is valid for all the municipalities concerned.

The tax in North-Rhine Westphalia extends to all entertainments as defined by the law, and a performance cannot fall outside this definition because it was not the organiser's intention to arrange an entertainment. Included are film, theatrical and musical performances, dances and sports events, fairs and cabarets. Exemptions cover a wider field than in the Netherlands, and extend to certain entertainments which are judged to be of a specially high artistic standard, of special cultural value or of special value in popular education. Furthermore, a specified lower or reduced rate of tax may be charged when such entertainments do not qualify for complete exemption but are of a high artistic, cultural or educational standard. Finally, the tax may be reduced, remitted or refunded in individual cases where special hardship is involved.

The adjudication of exemptions according to their educational or cultural value or artistic standard is the biggest problem in the administration of the entertainments tax. In Düsseldorf the Director of Taxes who takes the decision seeks the advice of qualified specialists in particular fields, as for example, a Professor of Music or the Director of Education. Where more than one municipality is concerned, the decision is taken by the *Land* Ministries. Films are, however, classified by a central body whose rulings apply to all municipalities in Western Germany. Puppet shows, which have given rise to considerable difficulties, are now entirely adjudicated by the *Land* Minister of the Interior in consultation with the Ministers of Finance and Education. Otherwise the administration, collection and inspection are in the hands of the municipalities and apparently give rise to no great difficulties. The costs of collection in Düsseldorf are estimated as 1 per cent of the tax yield.

There are two scales of tax, one for film performances and one for all other forms of entertainment. For films, rates are 25 or 30 per cent according to the price of admission, and the reduced rate for films of high educational, artistic or cultural standard varies from 10 to 22 per cent. For other performances, rates may be 15, 20 or 25 per cent according to price, with reduced rates of from 5 to 25 per cent. The rate is levied on the net price of admission. In certain cases, a flat rate

# NEW SOURCES OF LOCAL REVENUE

on the gross receipts of an entertainment may be levied. The municipalities must adhere to the scales of tax laid down by *Land* law.

As a result of representations made by the entertainments industry, particularly the cinema concerns, representatives of all provincial governments and of the associations of local authorities recently met together to draw up proposals for a new entertainments tax which it was hoped all provinces would then pass into law. The proposed law provides for standardised provisions regarding entertainments to be taxed and exempted from tax, reduces the discretion of the municipalities to introduce their own regulations governing the tax, and allows the tax to be levied on the gross or inclusive price of the entertainment. At the time of writing, a Bill modelled on these proposals is now being considered by the Parliaments of North-Rhine Westphalia, Bavaria, Hesse and Berlin. Three other *Länder*, Baden-Württemberg, Hamburg and Rhineland Palatinate, have already enacted laws based on the draft proposals. The three remaining *Länder* have not as yet taken any action. This move to standardise entertainments tax legislation indicates the dislike felt by the entertainments industry of variations in a tax which for over twenty years was imposed according to a uniform statute for all municipalities.

## YIELD OF LOCAL ENTERTAINMENTS TAXES

In both the Netherlands and Western Germany, the local entertainments taxes provide a relatively small but useful yield for the municipalities, and the greater part of it is derived from the tax on film performances.

The table below shows the yield of these taxes and of the Entertainment Duty in Great Britain as follows:

Yield	Netherlands (1953)		W. Germany (1953)		Gt. Britain (1954/55)	
	Million guilders	%	Million DM	%	£m	%
Total yield ..	23.8	100	143.9	100	41.3	100
Including:						
Cinemas tax ..	13.7	57	111.8	78	35.3	86
Other taxes ..	10.1	43	32.1	22	6.0	14
Per capita yield (approximate)	Fl. 2.26 = 4/2d.		3.09 DM = 5/2d.		16/8d.	

Sources: Centraal Bureau voor de Statistiek: *Bezoek an vermakelijkheidsinstellingen* 1953; Statistik der Bundesrepublik Deutschland: *Die kommunalen Finanzen im Rechnungsjahr 1953*; 46th Report of the Commissioners of H.M. Customs and Excise for the year ending 31st March, 1955.

## A LOCAL ENTERTAINMENTS TAX

The *per capita* yield of the tax is far higher in Great Britain than in the Netherlands and Western Germany, in spite of the fact that fewer entertainments are taxed and more qualify for exemption in Great Britain than in either of the other two countries. Free entertainments and those where the public are participants rather than spectators are not, for example, taxable in Great Britain. In Britain, duty paid on cinema admissions provides a very high proportion of the total receipts. Had the Entertainments Duty been a local tax in 1953-54, it would have met 3.3 per cent of current local expenditure in Great Britain in that year. This compares with a contribution of approximately 1.5 per cent in both the Netherlands and Western Germany.

### A LOCAL ENTERTAINMENTS TAX IN GREAT BRITAIN

Thus the experience of other countries has shown that an entertainments tax has been widely regarded as an appropriate source of local revenue, and where such a tax is adopted, no insuperable problems arise in connection with its administration. So far as our researches have gone, it is only in Great Britain and New Zealand that this tax has been used exclusively by and for the central government. It is not an instrument of economic policy, but rather a revenue raiser. The present yield of about £40 millions would be a useful addition to local authority revenues and the transfer would be simple enough to make.

The present tax rests on legislation and it would be necessary to give local authorities power to levy such a tax in place of the central government. We contemplate that such legislation would deal with the same kind of points covered by the present legislation and that it would include provisions calculated to preserve the main structure of the tax as it exists at the present time. The important points seem to us to be:

1. Which entertainments should be liable for tax and which, although within the scope of the legislation, should be capable of obtaining relief from payment of tax.
2. What provision should be made to prescribe different scales of tax for different kinds of entertainments.
3. What measure of discretion should be allowed to local authorities to determine the rate of tax payable.

We contemplate that there should be the same statutory provision for the different entertainments liable to tax as at present and the same provision for a right of appeal to the High Court on the question of



the interpretation of the Statute. During the last forty years a well-established case law has been built up on the important question of what constitutes an entertainment and we should therefore not expect any difficulty to arise on this head.

The present legislation provides for relief from tax of entertainments of various kinds, but only where the Commissioners of Customs and Excise are satisfied that certain conditions obtain. Generally speaking, educational and partly educational, scientific, amateur, and rural entertainments are accorded relief, and so are amateur games and sports, entertainments for the benefit of charities, for the furtherance of national pastimes, and exhibitions and agricultural shows. Applications for relief in the case of amateur games and sports and entertainments where the gross receipts are given to a charity without any charge on the takings are dealt with at the level of the thirty-two collection areas of H.M. Customs and Excise. All other applications are dealt with by the Head Office. We think it important that the question of relief should be dealt with throughout the country in a manner which is uniform and which does not involve substantial changes in a system which has become well established and well known to those engaged in the promotion of entertainment. It would seem to be administratively convenient for applications for relief to be addressed to and dealt with by local authorities, but we think that there should be provision for an appeal to a central body established for the purpose. We feel that if local authorities are made aware of the general lines of the policy to be adopted, there should be no great difficulty in dealing with individual cases. The question whether there should be any modifications in policy may be a matter for discussion in Parliament when legislation is introduced.

It is an important consideration in the grant of statutory powers to local authorities that there should be a measure of discretion to them in the exercise of the powers. There should, therefore, be some local flexibility in determining the amount of the tax. On the other hand, from the point of view of the presentation of legislation for such a transfer, it will be important to ensure that it should not be capable of leading to great increases in the incidence of the tax. The balance of advantage appears to lie in prescribing a statutory maximum somewhat higher than that already fixed for the type of entertainment bearing the highest rate, and leaving it to the discretion of local authorities to fix a lower rate where they think fit.

Under the existing legislation, provision is made for three scales of duty according to the type of entertainment. ("Live" entertainments, where the performers are present, such as the theatre; sports and racing;

## A LOCAL ENTERTAINMENTS TAX

and "mechanical" entertainments where the performers are not present, such as the cinema.) The lower rates of duty, and especially that on the theatre, have been determined by general considerations of policy. It seems to us that the fixing of differential scales has become an established part of the system and that the legislation should provide for the retention of this principle. We suggest that the legislation might prescribe the relationship that each scale of duty must bear to the others: for example, that the intermediate scale should be two-thirds of the top scale of the duty, and the lowest rate one-third. In view of the fact that 86 per cent of the present revenue from the entertainments tax is derived from cinemas, it is clear that from a revenue point of view, the dominant consideration will be the rate of tax fixed for this group of entertainments.

We should expect that the range of rates of tax would in fact not be very wide; in so far as there are variations in rates it would be easier for the industry to calculate prices over a wide area if the tax were imposed as a rate on the gross price of admissions (including the tax) instead of as at present on the net price of admission (exclusive of tax).

Local authorities would be entirely responsible for the administration and collection of the tax and would be given powers by the legislation to make bye-laws regulating such questions. The nature of the tax is such that the administration should not cause difficulties to the Treasurer's Department of local authorities whether big or small. A relevant consideration in this matter is, however, the fact that at present all entertainments held in sparsely populated rural areas are exempted from tax. In boroughs, urban districts, and rural parishes, the measure of population sparsity is taken to be fewer than 2,000 or 640 per square mile, and the entertainment may only be exempted when there are less than 400 seats in the building where it is to be given. As a result, the exemption is valid in all but a small number of the 11,000 rural parishes in England and Wales, and in some one hundred boroughs and urban districts besides. It would be a matter of policy to decide whether this exemption should be perpetuated in legislation which transferred from the government to local authorities the power to levy an entertainments tax, but in any case it must be expected that the chief *per capita* yields would be found in the bigger towns, as they are at present. The differentiation between areas would be reduced if the tax were levied at the county/county borough level and this would have the advantage in administrative counties of giving the county an independent income of its own.

While, therefore, we recognise that the largest amount of revenue

from this source is likely to be derived by authorities who already have the largest rateable resources and that the total yield of the tax is fairly small in relation to the total local authority income, our view is that any addition to local revenues is to be welcomed for the reasons we have already set out in our general consideration of local authority finances. Moreover, in the areas where the entertainments industry is an important one, the increased flexibility that the addition of a local entertainments tax would give would be a factor of some importance. The present entertainments duty is simply a means of providing revenue; it is not an instrument of national economic policy. We see no reason why such a tax which could without difficulty be levied locally should not be transferred to the local authorities.



## Chapter IX

### LOCAL TAXES ON ROAD TRANSPORT

SINCE motor vehicles first appeared upon the roads and taxes were levied on motoring, there has been controversy as to the proper use to which these revenues should be put, and the authorities which should receive them. This problem has been associated with the general question of which authorities should be responsible for financing road construction and maintenance.

In 1888, county council and county borough councils were made responsible for the building and upkeep of main roads. The first grants-in-aid from the central government towards the cost of maintaining roads had been made in 1882, but these and other grants were replaced in 1888 by a system of assigned revenues paid into a Local Taxation Account for redistribution to the local authorities. Among the revenues proposed was a "van and wheel tax," but this was never actually imposed. One of the taxes was, however, a duty on carriages. The Motor Car Act of 1903 required the registration and licensing of all vehicles and drivers, and it was decided that the proceeds of the licence fees should be assigned to the local authorities.

In 1909, an attempt was made to finance at least a part of road expenditure from motor vehicle taxation. The Development and Road Improvement Funds Act established a Road Improvement Grant and a Road Board. The Grant was assigned the proceeds of the motor vehicle licence duties levied at increased rates starting from £2 2s. od. per annum for a car of under 6½ h.p. and rising to £42 for a car of over 60 h.p., as well as the revenue from a new tax on petrol to be levied at the rate of 3d. per gallon. The Board was to assist in the building of roads by making payments from the Road Improvement Grant to local authorities and by building roads itself. During 1915-20, the Exchequer borrowed sums from the Grant, but these were largely repaid in 1920 and 1921. The Grant was reconstituted as the Road Fund in 1920, and it was now to receive the yield from licence duties on motor vehicles and horse-drawn carriages, and driving licences. The customs duty on motor spirit was repealed in 1921, and when it was reintroduced in 1928 (as part of a duty on hydrocarbon oils), it was not assigned to the Road Fund.

Meanwhile, the income of the Fund grew rapidly as the number

of motor vehicles increased, and the accumulating surplus proved too great a temptation for successive Chancellors of the Exchequer to resist in their search for general revenues. The first step was taken in 1926, when one third of the proceeds of certain motor vehicle licence duties were transferred to the Exchequer, and in 1927 and 1928 "raids" on the Fund to the extent of £6 million and £19 million were made. In 1935, it was decided to transfer any unspent balances from the Fund to the Exchequer. Finally, in 1937, all revenues were paid directly to the Exchequer and the Fund was henceforth financed by parliamentary vote. The fiction of a Road Fund was ended in 1955; all grants for road construction and maintenance are now included in the Ministry of Transport vote. As far as road expenditure is concerned, since 1937 the government has been responsible for building and maintaining trunk roads. The local authorities are responsible for all other roads and at present counties and county boroughs receive grants of from 50 per cent to 75 per cent towards the cost of building and, in the case of counties, maintaining certain roads "classified" by the Ministry of Transport.

Of a total public expenditure in Great Britain on roads and bridges of £90 million in 1953-54 (excluding loan charges), £58 million was borne by the local authorities, almost wholly from the rates, and £32 million by the central government, including expenditure on trunk roads and grants to the local authorities. Yet, in the same year, £311 million was raised from taxes on road transport, the whole of which accrued to the Exchequer. Of this, £288 million came from the tax on motor fuel and £73 million from motor vehicle licence duties. The revenue from motor taxation must be regarded as general revenue and we do not think it right to attempt to establish any direct connection between the revenue from road transport and expenditure on the roads. Nevertheless, looking at the obligations and powers of local authorities, we feel that the fact that they do incur so heavy an expenditure on roads entitles us to regard some form of motor taxation as falling within the field of local taxation. From this point of view we have considered whether any of the taxes on motor transport could properly be transferred to local authorities.

In the countries whose revenue systems we have surveyed, local authorities levy or receive a share of taxes on road transport in the U.S.A., South Africa, and Denmark. In the U.S.A., local authorities in five states levy a tax on motor fuel, at an average rate (in 1955) of 1.2 cents per gallon. This rate is in addition to rates imposed by the federal and state governments. In 15 states, local authorities levy taxes on motor vehicles, and the practice is most widespread in the state of

## LOCAL TAXES ON ROAD TRANSPORT

Illinois. There are also arrangements in many states for sharing the yield of state imposed taxes on road transport. Thus, 24 state governments share their revenue from motor fuel taxes with the local authorities, 12 share the tax on motor vehicles, and seven state governments have set up combined funds of all road transport taxes, from which shares are given to the local authorities. In Natal and the Transvaal, local authorities receive a share of the motor vehicle licence fees which are levied and collected in their areas by the provincial governments. In Denmark, the proceeds of state-imposed taxes on motor vehicles and a special tax on motor fuel are directed to the local authorities in the form of grants for road construction and maintenance and snow clearance.

### THE TAXATION OF MOTOR FUEL

In Great Britain a customs duty is levied on imported hydrocarbon oils at the rate of 2s. 6d. per gallon. In general, the price of motor fuel tends to be lower than in other countries of Western Europe. The greater part of the duty comes from oils which are used as fuel for motor vehicles. In addition, there is an excise duty levied on a small quantity of oils produced from indigenous shale or oil deposits and used as motor spirit, and on petrol substitutes, which is charged at the rate of 1s. 3d. per gallon. An exact calculation of the yield of all duties on oil used for motor vehicles cannot be given, but an estimate<sup>1</sup> made for Great Britain gives the figure as £253 million in 1954-55. The duty is collected on discharge from the tanker or clearance from the refinery—a simple and inexpensive method of collection.

If local authorities were given powers to levy such a tax there seem to be two possible methods of collecting it. First the oil companies could be asked to make returns to the local authorities in respect of deliveries in their areas. This would be simplest for the local authorities but it would impose a considerable burden on the oil companies. The alternative course would be for the local authorities to collect the tax from garages and petrol stations in their areas and from other users (e.g., transport concerns) who buy their petrol direct from the petrol companies. We think this method is preferable and we do not think that effective supervision should be impracticable if such a tax were imposed.

We consider that it is an essential characteristic of a local tax that a local authority should, within a statutory maximum, have a discretion in deciding the rate to be charged. With a motor fuel tax, there might

<sup>1</sup> See *Basic Road Statistics, 1955*, British Road Federation. This excludes duty on spirit used for aviation and industrial purposes.



be a certain amount of tax avoidance if there were a number of "no tax" areas adjacent to areas levying a tax. Our view is that if local authorities were given powers to levy such a tax, they would be exercised by most, if not by all, of them and that there would tend to be near uniformity in the tax rates. We do not think it likely that the extent of tax variation would be sufficient to make tax avoidance worth while. The number of local variations would be reduced if the powers were granted only to county and county borough councils, which is the course we would recommend.

If local authorities were given powers to levy such a tax it would either be an additional charge on the consumer or would have to be accompanied by some reduction in the rate of the customs and excise duties. We should not regard a local tax at a high rate as feasible, but if the tax were levied at a low rate of something like 2d. or 3d. a gallon it would not be impracticable. Its yield at the present time would be in the region of £10-20 million for England and Wales (£10-15 million at an average rate of 2d. per gallon and £15-20 million at 3d. per gallon). Such a revenue would be useful to local authorities, and might well benefit particularly a number of rural counties which are much visited by motoring tourists, have a relatively high expenditure on roads, and are heavily dependent on government grants towards the cost of their expenditure in general.

We see no reason to think that a tax on these lines could not be successfully administered. But it would not be possible to utilise the present central government administration to collect the tax, and this would mean that there would be two administrations working independently of one another both taxing the same subject matter. We realise also that there are considerations of general policy which might militate against allowing local authorities to impose a tax on petrol. The present level of taxation on road transport is very heavy and is the subject of much protest. Although, therefore, we feel that the possibility of a local tax on motor fuel should be seriously considered, we make no specific recommendations on this subject.

#### MOTOR VEHICLE LICENCE DUTIES

Motor vehicle licence duties are levied on all types of mechanically propelled vehicles, from motor cycles to private cars, lorries and agricultural vehicles. The present annual rates of duty vary between £9 and £12 10s. od. on cars, 17s. 6d. and £5 on motor cycles, and £6 and £90 on goods vehicles according to the unladen weight of the vehicle and the use to which it is put. Since 1954, an additional transport levy has been imposed on certain types of goods vehicles as part

of the denationalisation measures but there is a proposal at present before Parliament to abolish this by the end of 1956. The licence duties are collected on behalf of the Ministry of Transport by the counties and county boroughs, which are also responsible to the Ministry for registering the vehicles. Certain licences may be renewed by paying the fee to the Post Office instead of to the local authority. The money collected by the Post Office is paid into the central Motor Taxation Account, but the Local Taxation Officer of each county and county borough is informed of all licences issued in respect of his area, and the information is incorporated into the monthly returns his authority makes to the Ministry of Transport. About 90 per cent of the total duty is collected by the local authorities. The total yield of motor vehicle licence duties in Great Britain was £73 million in 1953-54 and £79 million in 1954-55.

The transfer of the right to levy the motor vehicle licence duties to the local authorities would simply mean that the counties and county boroughs would act as principals instead of agents in the administration of the tax. The yield of the duties is a stable one, and, as the number of cars and lorries on the road increases, it will prove an expanding source of revenue. The yield per head of population varies considerably as between one authority and another. While the average is in the region of £1 10s. od., in some areas the yield is well over £2, and in others as low as 16s. od. This is illustrated by the figures in the table on page 112. Costs of collection, which are also shown in the table, are relatively small.

If the duties were levied by the local authorities, it would not be possible to allow owners of vehicles to pay duty in the area of their choice, as this would result in widespread tax evasion in areas where rates were high. The law would have to specify the local authority area to which the duty should be paid. The simplest and most practicable general rule would be for payment to be made to the area where the vehicle is normally kept and from which it is therefore operated.

The present practice adopted by many large organisations of registering all their vehicles with one local authority would however present a considerable problem. The London Midland Region of British Railways, for example, pay licence duties amounting to some £200,000 for all their vehicles to the County of Hertford. In the County of London, some 75,000 licences, or nearly one fifth of the total number of vehicle licences issued, are for "central registrations"; the vehicles may not be operated from London at all, but the licences are paid there because the headquarters of the organisation owning the vehicles is

# NEW SOURCES OF LOCAL REVENUE

REVENUES IN 1954/55 FROM VEHICLE LICENCES IN CERTAIN COUNTY BOROUGH  
AND ADMINISTRATIVE COUNTIES

	Gross Revenue collected by Local Authorities and Post Offices	Number of Licences	Cost of Collection by Local Authorities		Revenue per Head of Population
			Percentage of Revenue collected by Local Authority	Pence per Licence issued by Local Authority	
(a) County Boroughs	£'000	'000			£
Birmingham	2,313.1	469	2.03	25	2.07
Blackpool ..	234.3	60	2.31	22	1.59
Burnley ..	122.7	24	2.53	31	1.48
Merthyr ..	49.8	13	1.57	14	0.84
Oxford ..	277.9	66	2.51	26	2.60
(b) Counties					
Middlesex ..	3,833.8	1,071	4.46	37	1.70
Oxfordshire	366.0	114	2.62	20	1.93
Suffolk, West	269.0	72	2.77	25	0.80
Yorkshire, W. Riding	2,068.4	563	2.39	22	1.29

in London. Most of these central registrations consist of large fleets of lorries and coaches and the value of their licence duties is therefore relatively important to the total. Because such duties are only paid to a particular local authority for the sake of convenience, that authority would in equity have no particular claim to the whole of the revenue. It would be possible to provide for registration and payment of duty to be made in the area in which each vehicle was kept, but this solution would mean that very substantial revenue would accrue to those authorities with large transport garages in their area. In our view,



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however, this is the best answer. An alternative approach would be to provide for the payment of the duty in these cases to a Municipal Fund from which it would be distributed among the local authorities. If the latter course were adopted, it would derogate from the merit of the tax as a local tax.

As far as the rate of the tax is concerned, it would not be possible to give local authorities unfettered discretion in determining the rates of duty they proposed levying, for too great a variation in rates would not be acceptable to vehicle users. A maximum permissible rate would, therefore, have to be set by law.

Our conclusion is that vehicle licence duties might well be transferred to the local authorities, and they would constitute a very useful addition to local authority revenues. As a local tax, the yield would have contributed 7 per cent to rate fund revenues in 1953-54. It would, however, almost certainly be necessary for the central government to limit very closely the discretion local authorities could exercise in determining rates, discriminating between various classes of vehicles and so on. For this reason, while we regard motor vehicle duties as suitable for transfer to local authorities, we would not regard them as our first choice for a new local tax.

## DRIVING LICENCE FEES

Driving licence fees, like motor vehicle licence duties, are at present collected by county and county borough councils as agents for the Ministry of Transport and Civil Aviation. The yield in 1955 was £2.6 million for Great Britain. The right to levy the duties could easily be transferred to the local authorities, subject possibly to a statutory maximum rate. The duty would be paid by the driver to the local authority area in which he lived, and there would be no administrative problems similar to those arising from the central registration of motor vehicles. The present licence fee is 5/- per annum, and this is the same as when the duty was first imposed in 1903. In recommending the transfer of driving licence duties to the local authorities, we have in mind that local authorities should be given discretion to levy a rate substantially higher than this.

## PARKING METERS

Parking meters are extensively used in the cities of the U.S.A., and in many cases the revenue from the fees is used for general revenue purposes. For example, revenue from parking meter fees provided between 3 per cent and 5 per cent of the total revenues of nine first-

class cities in Kansas over the period 1949-52.<sup>1</sup> Parking meters are also in use in some Canadian cities, in Auckland, Stockholm, and in some towns in Western Germany. Under the terms of the Road Traffic Bill at present before Parliament, a number of parking meters will be set up for experimental purposes in a district of London. Any profits from the meters are to be used by local authorities to finance "off-street" parking places. If they are to be adopted generally in this country, the revenues accruing from them ought clearly to go to the local authorities, which are the public authorities chiefly concerned with traffic regulation and parking problems. But parking meters should in our view be regarded primarily as a means of regulating parking, rather than as a means of providing revenue for general use.

<sup>1</sup> See *Municipal Finance—a study of nine first-class cities*, H. O. Lawson, Governmental Research Center, University of Kansas.

## Chapter X

### A LOCAL SALES TAX, POLL TAX, AND MISCELLANEOUS TAXES

A sales tax may be imposed either on the manufacturer, or on the wholesaler or on the retailer. The ultimate incidence of a sales tax is, broadly speaking, on the consumer. A sales tax at the manufacturing or wholesale level would not, in our view, be suitable for local imposition as much of it would ultimately fall on people who neither lived nor worked in the area covered by the local authority imposing the tax. It follows that if a local sales tax were to be imposed, it would have to be imposed at the retail level. It is in this context that we have considered the matter in the present Chapter of our Report.

Local retail sales taxes are found in the Province of Quebec in Canada and in 10 states of the U.S.A., most notably in California, Illinois and New York. The first local sales tax was imposed by New York City in 1934. It was followed by Montreal (1935), New Orleans (1936) and the City of Quebec (1940). After 1945, development was rapid, and by 1955 taxes of this kind were levied in the U.S.A. by some 900 municipalities, 171 of which had a population of over 10,000. Over half of all Californian cities were imposing local sales taxes in 1955. In the same year a striking development occurred in Illinois where local authorities were granted powers to levy local sales taxes without having to seek prior approval from the voters at a referendum. Within six months, 617 urban authorities, including Chicago, had imposed the tax at a rate of  $\frac{1}{2}$  per cent. A number of cities in the other states, most notably New York, Louisiana and Mississippi, levy a local sales tax, but the development is very largely confined to the biggest cities. In Canada, local sales taxes are at present imposed by twenty-three of the twenty-seven cities with a population exceeding 15,000 and by nearly half of the cities with a population of between 2,000 and 15,000 in the Province of Quebec. It is important to bear in mind that where a local sales tax is imposed, there is nearly always a state or provincial sales tax. The two exceptions are New York and Virginia where no state sales tax is imposed.

The estimated yield of local sales taxes in the U.S.A. in 1955 for cities with a population exceeding 10,000 was \$392 millions, and the



average *per capita* yield was \$16. New York City alone levied \$221 millions in 1953-54, with a *per capita* yield of nearly \$30. In Quebec Province municipalities levying local sales taxes raised \$24 millions, and school boards a further \$10 millions in 1952-53. Sales tax contributed 20 per cent or more of the total taxation of cities in Quebec with a population exceeding 15,000 which levied a tax in 1952-53.

There is some variation between one authority and another as regards the goods (or services) which are chargeable to tax. In New York City, for example, the tax extends to the retail sales or rental of all tangible personal property, and also to certain services such as gas and electricity. Most cities exempt all or some food products from tax, and other exemptions usually include sales by or to the government, sales to hospitals, and, to avoid multiple taxation, sales of commodities which are to be embodied in the final product of a manufacturing process. In addition, sales to people resident outside the city imposing the tax are often exempt.

A "compensating use" tax, levied on all goods brought into the local authority's area which are not intended for resale is often levied by cities imposing the tax. The aim is to prevent tax evasion by residents and to protect the cities' traders from competition from areas where there is no sales tax. But it is found in practice that the use tax can only be enforced in respect of large items such as cars. The yield from the use tax is comparatively small; in New York City in 1950, it raised \$1.6 millions against sales tax revenue of \$132.2 millions.

Rates of sales tax vary from 3 per cent in New York City and Montreal (city and school taxes) to  $\frac{1}{2}$  per cent in Illinois and Mississippi. Of the 188 Californian cities levying the tax at the end of 1955, 155 levied a rate of 1 per cent, 32 levied  $\frac{1}{2}$  per cent, and one city  $1\frac{1}{2}$  per cent. Where the state or provincial authorities also levy a retail sales tax, the combined rates may be as high as 5 per cent.

The tax may be imposed as a matter of law either on the purchaser or on the retailer. In either case, the retailer is responsible to the authorities for the collection of the tax, and in some cases receives a commission for this work. In Canada, the provincial government collects the local tax with its own provincial tax, and remits it to the local authorities after deducting a collection fee. In the U.S.A., the tax is collected by the local authorities in California, New York, and five other states. In Mississippi, Illinois and New Mexico the state government collects the local tax together with its own sales tax. As from April, 1956, Californian cities may ask the state to collect their sales taxes for them.

There appear, however, to be serious administrative problems,

#### A LOCAL SALES TAX, POLL TAX, AND MISCELLANEOUS TAXES

especially where a large number of local authorities within an area all impose a local sales tax. These problems have been encountered particularly in California, where every local authority levying the tax has its own ordinance establishing what is to be taxed and what exempt, and tax rates vary between areas. For effective administration it is necessary for the collecting authority to compile and keep up to date a register of all retail outlets in its area. It must then collect and analyse returns from the retailers at quarterly intervals at least. To minimise tax evasion it is desirable that returns should be audited. Finally, in cases of default, payments of tax must be enforced. All of these operations are likely to be more difficult and costly than, for example, the administration of a local tax on land and buildings. Few of the Californian cities levying the sales tax have instituted audit systems, contenting themselves with self-assessment by the retailers. The result has been a loss of about 30 per cent of revenue compared with the yield of the state sales tax where there is an audit. The costs of administration for sixty-four Californian cities levying the tax in 1950-51 have been calculated, and it was found that the mean cost was 2.7 per cent of the tax receipts, but that costs rose to between 6 and 9 per cent in some cases. The cost of collecting the state sales tax in 1949-50 was 2.1 per cent, but nearly half of this comprised auditing costs. Thus the state collection costs were considerably lower than the local collection costs, even though the great majority of the cities did not have to bear the comparatively heavy expense of audit.

A further difficulty arises from the different rates levied and the variation in local tax ordinances. These factors greatly increase the work of the retailer, especially in the case of multiple stores where separate returns must be made to each local authority. For every sale for delivery in another local authority area, the vendor must discover whether the commodity sold is taxable under that authority's ordinance, and if so, at what rate. Compliance with the tax is thus both complex and costly. Another result of differing tax rates tends to be a distorted location of shopping centres, i.e., shops are set up in suburban areas where there is no tax or where the rate of tax is lower. This will affect adversely the shops in the area of high tax rates, and also cause a fall in that authority's tax revenues.

A number of leading tax reports and authorities<sup>1</sup> have therefore concluded that a sales tax is best administered at the state level, and

<sup>1</sup> See *The Tax Problem*, Report of the Tax Study Committee, Commonwealth of Pennsylvania, 1953; J. F. Due, *Government Finances*, 1954; *Report of the Senate Interim Committee on State and Local Taxation*, Part II: State and Local Sales and Use Taxes in California, 1953; D. L. Pierce, "City Sales Taxes," *Canadian Tax Journal*, November-December, 1953.



some also think that it should be levied by the state and shared with the local authorities.

#### A LOCAL SALES TAX IN GREAT BRITAIN

We accept in general the criticisms that have been made about the administration of a sales tax at the local level. In Great Britain, the concentration of urban population in areas administered by a number of different local authorities would accentuate the problems arising from differing tax rates between local areas, which have been outlined above. Moreover, if the tax were to be imposed by local authorities in Great Britain, a high standard of administration would be expected, and this would certainly increase the administrative costs.

A bigger obstacle to the imposition of a local sales tax in Great Britain is the existence of the purchase tax imposed by the central government. This tax is levied at high rates, and on a comparatively restricted range of goods. If a local sales tax were also levied, there would be considerable pressure to exempt from tax all the goods accorded relief from purchase tax. If this were done, either the yield of the tax would become relatively insignificant, or sales tax rates would be forced up to bring in the necessary revenue and the result might be two taxes of high rate on the same goods. But low rates of tax are essential to the successful operation of a local sales tax so that it is not worth the shopper's while to transfer his custom to another area where the rates are lower.

Furthermore, the purchase tax is levied at the wholesale level. For the reasons given at the beginning of this chapter, it would be neither desirable nor practicable to levy a local sales tax at the wholesale level. This would mean that while the purchase tax would be collected from wholesalers, local sales taxes would be collected from retailers. It would not, therefore, be possible to provide a uniform administration and collection of the two taxes.

Our recommendation is therefore against the introduction of a local sales tax in Great Britain.

#### A LOCAL POLL TAX

Poll taxes are imposed by local authorities in five of the Canadian provinces. In New Brunswick they contributed 16 per cent of all local taxation in 1953. Poll taxes are also levied by some cities in eleven states of the U.S.A., but except in Pennsylvania the practice is not on the increase and the yield is minor in relation to the total revenues of the authorities imposing them. Receipts from local poll taxes in Switzerland amounted to 1 per cent of total local taxation in 1953.



## A LOCAL SALES TAX, POLL TAX, AND MISCELLANEOUS TAXES

Examples of poll taxes are those levied on all adults, on householders or on men only; in some cases the tax is levied only on those who have paid no other local taxes.

A poll tax is a simple tax, easy to collect and with a steady, if small, yield. It secures a contribution towards local expenditure from people who do not pay other taxes. But we do not believe that a poll tax would be acceptable in this country. It is a crude taxing instrument which makes no differentiation according to means or family circumstances. Any attempt to modify it to take these factors into account leads straight to an income tax, which we have already discussed.

### MISCELLANEOUS TAXES

A variety of minor taxes are imposed by local authorities in other countries. In France, local authorities have optional powers to levy a number of taxes on items of expenditure, such as carriages and horses, clubs, pianofortes and organs, hunting rights, balconies, personal servants, furnished lodgings, and spa waters. In the Netherlands, local authorities may levy taxes on poster advertisements and on the market value of building sites. In Western Germany, local taxes are levied on hunting and on beverages sold in cafés, and in Switzerland on hotels, musical instruments, servants and posters. In Switzerland also, gains from the sale of land and buildings and other property may be taxed in certain cantons, and stamp and death duties are levied by some local authorities. In no case is the yield from these taxes important in relation to total local revenues. These minor taxes may be of interest to particular local authorities, but in general we do not think that the likely yield would justify the trouble and expense of administering them.

### EXCISE LICENCES

Excise licence fees, which are charged to provide revenue for general purposes, may be distinguished from fees charged for licences where the fee is intended only to cover the costs of administration. The excise licence fee is really a tax linked to a licence. Taxes on businesses, on motor vehicles, on dogs, and on the sale of liquor are often charged in this way.

We have dealt with the possibility of transferring motor vehicle licence fees to the local authorities in Chapter IX. We have also considered the liquor excise licence duties which are at present levied by the central government on all retailers of spirits, beer and wine. The net yield in Great Britain of £4.3 millions in 1945-55 accrued to the Exchequer, and the duty is administered by H.M. Customs and Excise. These licence duties are payable only by those who have

## NEW SOURCES OF LOCAL REVENUE

obtained a Justices' Certificate under the provisions of the Licensing Act of 1910, and the sum levied is generally a percentage of the annual value of the premises used (according to the Schedule A valuation). Such licences might perhaps be granted by the local authorities, and the yield from them is likely to increase as valuations are revised. The sum involved is a small one, and, like other minor taxes, it is doubtful if the yield in individual local authority areas would be worth the trouble and expense of administering the duties.

## Chapter XI

### ASSIGNED REVENUES AND A MUNICIPAL FUND

OUR study of supplementary sources of revenue would not be complete without some reference to assigned revenues in view of the part which they formerly played in local government finance in this country and which in different forms they still play in a number of other countries.

Assigned revenues were introduced in this country by the Local Government Act, 1888. They were designed to provide assured contributions towards the general relief of local rates. The essential idea underlying the Act was that instead of one common purse there should be two distinct and separate purses, one for Imperial, the other for local, purposes. The latter purse was to be filled to some extent in a more equitable manner than resulted from reliance solely on rating by the transfer to it of some of the contents of the Imperial purse. Under the Act a Local Taxation Account was created into which were paid receipts from licences for the sale of intoxicating liquors, licences for tobacco, dogs and guns, and specified proportions of the death duty grant and of the beer and spirit surtaxes.

It was contemplated that under this scheme the resources of local authorities would be automatically increased, the yield of the assigned revenues being likely to increase as years went on. This expectation was, however, defeated by subsequent decisions to substitute fixed annual payments for the flexible payments which had been contemplated in 1888. Experience thus showed that the system of surrendering potential sources of revenue to local purposes was liable to be overthrown to meet the exigencies of Imperial taxation. The separation of local and national revenues which was envisaged by the authors of the system of assigned revenues ceased to be a reality and this system became, for all practical purposes, one of grants from national revenues as a whole, fixed and distributed in a special manner.

These grants were distributed for the most part by way of contributions to specific services, but the total amount of grant available for distribution was governed not so much by circumstances relating to the particular service as by the amount of money deemed to be available from the assigned revenues.

When the system of assigned revenues was introduced, the specific



# NEW SOURCES OF LOCAL REVENUE

grant for elementary education was retained and continued to be given on a basis which was primarily related to cost.

The system of exchequer grants, including that of assigned revenues, was examined by a Royal Commission under the Chairmanship of Lord Balfour of Burleigh<sup>1</sup> which reported in 1901, and by the Departmental Committee under the Chairmanship of Sir John Kempe<sup>2</sup> which reported in 1914. The Majority Report of the Royal Commission recommended the retention of the assigned revenues system in a modified form. The Minority Report criticised the system, as did the Kempe Committee which recommended its abolition and its replacement by a system of block grants towards the cost of particular services to be calculated on a basis which combined units (so much per head) with expenditure.

Although the assigned revenues were not abolished until 1929, the general policy followed in regard to government grants during the extension of local government services following the 1914-18 war, was based on the principle of grants for services. The transformation which took place in regard to the distribution of grants is illustrated by the following figures:

<i>Year ended 31st March</i>	<i>Specific grants for education</i>	<i>Assigned revenues</i>	
		<i>Specific services</i>	<i>Non-specific</i>
	£000,000	£000,000	
1891	1,445	6,009	
1911	12,578	5,504	2,861
	(from voted money)		
1929	77,333	8,116	6,444

An important part of the Local Government Act, 1929, was the introduction of a new unallocated grant which took shape in the General Exchequer Contribution and the proposals were based on the view that the unallocated grants formerly payable under the assigned revenues were both badly distributed and inadequate.

Although there was general agreement at that time that the assigned revenues system as then operated was inadequate and inappropriate and no further proposals for such a system have, so far as we are aware, been made, we do not think that in a search for supplementary sources of revenue for local government they should be excluded from consideration.

<sup>1</sup> Royal Commission on Local Taxation, 1899-1901, C 9141/2 and Cd. 638.

<sup>2</sup> See page 81 n.

## ASSIGNED REVENUES AND A MUNICIPAL FUND

One possible method of meeting criticism against the previous system of distributing assigned revenues might be to arrange for their distribution through a Municipal Fund. Municipal Funds exist in a number of other countries, notably in the three Scandinavian countries, the Netherlands and France, and it is interesting to examine the way in which they are operated.

- (i) *The Municipal Equalisation Fund in Denmark* is financed by the annual yield of a special tax on land and buildings and a share of the central government taxes on individual income and property which in 1956 replaced the former special tax on income. It makes grants to the municipalities in aid of public assistance, pensions, schools, and hospitals, and there is a special sum of kr. 1 million annually available for grants to municipalities in special difficulties. The Fund is administered by the Ministry of the Interior. If the Bills presented to the Danish Parliament in 1954 are passed, the Fund will be abolished and its revenue and expenditure will be taken over by the central government. There will, however, be a Municipal Grants Fund financed by the capital of the Municipal Equalisation Fund and a new surtax on income, which will accumulate money to assist municipalities in times of financial difficulty.
- (ii) *The Swedish Tax Mitigation Fund*, which is administered by the central government and managed by a board on which the local authority associations are represented, is financed by that part of the local income tax levied on income earned in Sweden by non-residents, and also by central government taxes. Grants from the Fund are made according to a formula, and the aim is to raise the financial resources of certain authorities to a minimum standard. The grants are in this respect similar to the Exchequer Equalisation Grant in the United Kingdom. The sums received are not of great importance to local revenues as a whole.
- (iii) *The Tax Equalisation Fund in Norway* is administered by the Ministry of Local Government and makes grants to municipalities with a heavy burden of taxation and low standards. The Fund is financed by the central government (over 50 per cent) and by one half of the local surtax on income, the whole of the local surtax on shipping companies, and the interest on the Fund's capital.
- (iv) *The Municipal Fund in the Netherlands* is administered by the



Ministry of Home Affairs with the help of an Advisory Council on which local authorities are represented.

The Fund is financed by percentages of the yield of the main national taxes, and these percentages are voted by Parliament. Grants from the Fund supply over 40 per cent of the revenue of the Dutch municipalities as a whole. Grants are made towards the salaries of the mayors and town clerks, and there are general grants based on expenditure on certain services and on the yield of the surcharge on the enterprise tax which previously accrued to the municipalities.

- (v) *The Equalisation Fund in France* is financed by a percentage of the yield of a general sales tax, the rate of which is fixed by Act of Parliament (not the Budget). The Fund is managed by a committee of nineteen, of which fourteen members are elected by the local authorities, and it makes grants to the Departments according to formulae taking into account many factors which reflect the comparative needs of authorities. The Departments then re-apportion the sums received among their communes. The amounts involved are not of great importance to local revenues. There are also a *Road Fund* and a *School Fund* financed by percentages of national taxes. The amount given to the municipalities within each Department is decided by the General Council of the Department.

Central government municipal funds have been found to be valuable where State revenues are to be assigned to local authorities, and they might well be used for a similar purpose in this country. We have, however, expressed the opinion below that assigned revenues should not be employed in this country except as a last resort. We should hope, therefore, that municipal funds would not be needed to any great extent in this connection. Municipal funds can, however, be used for somewhat different purposes and we hope their wider possibilities will not be ignored. The idea of municipal funds is not altogether unknown in England, in as much as payments to local authorities in lieu of rates on electricity and freight transport hereditaments take the form of a share of a national pool, fed by contributions made centrally by the industries and distributed to individual local authorities according to the rateable value of the hereditaments in their areas. We cite in our report two instances of the possible incidental use of municipal funds. The first is in connection with the central assessment and collection of local income tax in particular cases. Secondly, we mention that an alternative way of dealing with the income from the licensing of large



#### ASSIGNED REVENUES AND A MUNICIPAL FUND

fleets of vehicles, which for convenience are registered centrally, would be for the money to be paid into a central fund from which it would be distributed to local authorities. We consider that local authorities should as far as possible be allowed to manage municipal funds themselves.

So far as assigned revenues themselves are concerned, we do not think that they represent as desirable a form of local revenue as local taxes whose rate is determined by the local authority, since the scope of any assigned revenue will be determined by circumstances outside the control of the local authority. We should regard the possible buoyancy of an assigned revenue as an advantage for a supplementary source of income for local authorities, but this advantage would be lost if, as happened under the previous system (and again under the Road Fund), fixed payments were substituted in place of expanding revenues.

## Chapter XII

### RECOMMENDATIONS

THE main purpose of our enquiry has been to find ways of halting the continuous trend to increased dependence on central government by making available to local authorities increased revenues at their own disposal. It seems to us axiomatic that a central government, having set up independently elected local authorities, should allocate the taxable resources of the country in a way which would give its local authorities sufficient independent revenues of their own. How far practice in Great Britain falls short of the ideal has been shown in the preceding pages, and by the report of the International Union of Local Authorities Rome Congress to which we referred in Chapter IV. The collection centrally of so much money for subsequent filtering to the local authorities through an elaborate grants system is expensive, irritating and out of harmony with the principles of local self-government.

We do not think that our objective is likely to be secured within the ambit of the existing sources of revenue. We cannot foresee any material increase in the revenue from fees, rents, recoupments, etc. Revaluation will make no real contribution to solving the problem of more revenue for local authorities. Ratepayers are concerned mainly with the amount of money they are asked to pay, and the objection to increased payments will be the ultimate determining factor. We have recommended the abolition of derating, for our view is that if any assistance is to be given to industry and agriculture for reasons of national policy, provision should be made from the National Exchequer and not at the expense of the local authorities. Re-rating will broaden the basis of rating and result in a higher yield from the rates, particularly in some districts, but it is a gain which cannot be repeated and it will not in itself be sufficient for our long-term purposes. It will bring only a breathing space for local authorities, a temporary solution before the whole problem of finding further revenue would have to be faced again. Nor is it any solution to suggest that certain services be taken away from local government. What is required are new supplementary sources of revenue which will enable local authorities to discharge the services which are appropriate for administration by them.

The imposition of any new tax is likely to give rise to opposition

## RECOMMENDATIONS

both because some people will be adversely affected and because it will bring new legal and administrative problems in its train. This may be the more so in the case of new local taxes because of variations as between one area and another. To the natural complaint about national taxes "Why should I have to pay?" is added the further complaint "Why should I have to pay when people living in . . . . . don't?" The easy course is to leave things as they are and to continue to rely on the rates. The rates are a well tried and tested instrument; their yield is large and stable; and their anomalies, while serious, are old and accepted. We would not subscribe to the view that the rating system is breaking down or is in any danger of so doing. What we do think is that so long as local authorities continue to rely exclusively on the rates, the present pronounced trend to greater reliance on central government grants will continue and this must bring with it an increasing measure of central government direction and control. Whether this is a good or a bad thing is a matter of personal opinion and judgment. But we do think that it ought to be realised that a decision in favour of continued exclusive reliance on the rates is a decision in favour of growing dependence on the central government. This is the issue that must be faced. We are under no illusion that the imposition by local authorities of one or other of the alternative taxes we have reviewed would be either popular or easy. But this is the price that may have to be paid to preserve the independence of local government.

The taxes we have reviewed as potentially suitable for local adoption in this country fall into two groups:

- (i) Taxes suitable for transfer by the central government to local authorities. Perhaps a better way of expressing this would be to say that the government would vacate certain fields of taxation in favour of local authorities.
- (ii) Taxes suitable for imposition by local authorities independently of national taxation.

Clearly the first group would give rise to the least opposition on the part of the taxpayer and would present the fewest administrative problems. To the natural reluctance of the central government to surrender some of its own taxation there is the answer that it would probably have to find the money anyway—if not by concession of taxing powers then by grants to local authorities. The outstanding example is the Entertainments Duty and we would regard this as our first choice in this group if local authorities are to be given additional taxing powers. Driving licence fees are also suitable for transfer to



local authorities, although the yield is too small to be of major importance. Because of the difficulties presented by large transport fleets, we would not regard the motor licence duties as a first choice. None of these taxes is of primary importance from the economic point of view, and their transfer to local authorities would not diminish the government's control over economic affairs.

In the second group, the outstanding example is the local income tax. We do not minimise the difficulties to which this would give rise and, indeed, we feel that it could only be operated successfully if it were confined to personal incomes. If on grounds of equity it were felt essential that company undistributed profits should be brought in, we are convinced that this could only be done by some special device, e.g., by central assessment and payment of the tax into a Municipal Fund which would then be divided up among the local authorities; or by empowering local authorities to levy an additional rate poundage or other charge on companies. Nevertheless, the yield of a local income tax would be very substantial, even if imposed at a modest rate and on personal incomes only—possibly for the country as a whole £150 million on a 3d. rate—and this is the only measure which on its own offers a prospect of a long-term solution of local authorities' revenue problems.

When the time comes, as we are sure it will, to broaden the base of local authority revenues, we recommend the following as practicable sources of additional revenue. We have arranged them in the order of our preference, and we think that the case is stronger for the first two than for the last one.

- (i) Local authorities should be given power to impose a local income tax. We think as a matter of administrative practicability that this would have to be confined to personal incomes and that undistributed company profits would probably have to be excluded, but in that event we recommend that steps be taken to impose an equivalent charge on companies. The Act should provide for a maximum rate of tax of 3d. in the £.
- (ii) Local authorities should be given powers to levy an entertainments tax subject to the central government providing by statute (a) for the maximum rate of duty to be chargeable, and (b) for the relationship between the scales of duty applicable to different classes of entertainment. This new local tax would replace the duty at present levied by the central government.
- (iii) Motor vehicle duties and driving licence fees should be transferred to local authorities and the present duties withdrawn.

## RECOMMENDATIONS

We have considered the possibility of a local tax on motor fuel, and, while we do not consider it impracticable, we make no specific recommendation on the subject.

We have reviewed, we believe, virtually the whole field of other potential local taxes, but whatever experience abroad may be, we do not regard any as suitable for adoption in this country either because conditions here are such that we do not regard them as practicable, or because their yield is insufficient to justify the work and disturbance they would create.

We recognise that the largest amount of revenue from the taxes we recommend will usually be derived by the local authorities who are already in the strongest financial position. We have to admit that we have been unable to find any tax which would painlessly and equitably raise the largest amount of revenue in those areas which are at present most dependent on government grants; but if our proposals for the rating of industry and agriculture are accepted, it would make a big difference to many areas which are at present most dependent on government grants. The purpose of seeking alternative sources of revenue is to reduce the dependence of local upon central government. The provision of a revenue of £100 million to £200 million which will be widely spread through the country, would have a substantial influence in this direction, and the fact that it would give some authorities more revenue than others, does not in our view detract from the advantages of the proposals. We would not assume that all local authorities would wish to levy the new local taxes we have recommended. What we have in mind is that they should have discretion to choose for themselves among a number of taxes at their disposal, and to use them in the way best suited to their individual needs. They would thus no longer be exclusively dependent on the rates although some authorities might well decide for a period of years at any rate that their interests would best be served by continuing to raise the whole or the greater part of their revenue through the rating system. But local authorities would no longer find themselves in the position they are in at present where they can only finance their services by continual increases in the rate of the solitary tax at their disposal. We recognise that the adoption of the proposals will require a review of the existing arrangements for the payment of government grants, and we should assume that in any revised arrangements for grants towards the general cost of local government, the government would take account of the extent of the financial sources available to local authorities at their own disposal.



Our proposals do not involve any increase in the amount of money to be raised for government purposes, either central or local. Indeed, insofar as an elaborate grant system is expensive to administer, they would bring some small savings. If the cost of local government is to increase, it will be as the result of changes in the scope of local government services or the scale on which they are carried out, or of changes in the price level. These result from economic conditions and decisions on social policy, which are outside our province. It is, however, a matter of historical fact that over a long period of years, the cost of local government has continued to rise, and the ability of local government to meet this cost out of resources at its own disposal has continued to diminish. We note also the avowed intention of the main political parties to continue in the future to rely on local government for a wide range of services and we think that under the present conditions, it would be unrealistic to look forward either to a reduction of local government expenditure, or to a readiness to put a greater proportion of this expenditure upon rates. What we have been concerned with is to find what we conceive to be better ways of distributing the financial burden which will have to be met in any case, and we are confident that this result will be secured by the adoption of our recommendations.



# *The Finance of Local Government in Sweden*

A description of the structure, functions and  
finance of local government in Sweden with  
particular reference to the local income tax,  
and a brief study of the possibility and effects  
of instituting a similar type of tax in the  
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Our proposals do not involve any increase in the amount of money to be raised for government purposes, either central or local. Indeed, insofar as an elaborate grant system is expensive to administer, they would bring some small savings. If the cost of local government is to increase, it will be as the result of changes in the scope of local government services or the scale on which they are carried out, or of changes in the price level. These result from economic conditions and decisions on social policy, which are outside our province. It is, however, a matter of historical fact that over a long period of years, the cost of local government has continued to rise, and the ability of local government to meet this cost out of resources at its own disposal has continued to diminish. We note also the avowed intention of the main political parties to continue in the future to rely on local government for a wide range of services and we think that under the present conditions, it would be unrealistic to look forward either to a reduction of local government expenditure, or to a readiness to put a greater proportion of this expenditure upon rates. What we have been concerned with is to find what we conceive to be better ways of distributing the financial burden which will have to be met in any case, and we are confident that this result will be secured by the adoption of our recommendations.

# *The Finance of Local Government in Sweden*

A description of the structure, functions and  
finance of local government in Sweden with  
particular reference to the local income tax,  
and a brief study of the possibility and effects  
of instituting a similar type of tax in the  
United Kingdom

A. L. IMRIE

City Chamberlain, Edinburgh

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## INTRODUCTION

WE arrived in Stockholm on 20th September, 1954, and spent eighteen days in Sweden. We had upwards of twenty conferences with representatives of local authorities' organisations and government departments.

We are particularly indebted to Professor Heckscher, the Director of the Swedish Institute, and to his staff who placed their great knowledge and experience at our disposal. We also received the most valuable assistance from Mr. Filip Anger, the President of the *Sveriges Kommunal tjänstemanna-förbundet*, and from Mr. Åke Sjöqvist, the Secretary.

We were accompanied in our investigation by Mr. Cecil Stout, of the City Chamberlain's Office, Edinburgh, whose assistance was of great value. Preparatory to travelling to Sweden we made a preliminary study of the subject, in which we were assisted by Mr. W. Hayhurst, City Treasurer of Westminster, and by the Foreign Section of the Library Staff of the Board of Inland Revenue, to whom our thanks are due. We also wish to pay a tribute to Mrs. Enid Wistrich, whose efficiency in arranging our visit and making our preliminary appointments contributed so much to the success of the investigation.

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### *Local Authorities*

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## INTRODUCTION

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Uppsala Town Council.	Drätselldirektör N. A. Wahlgren; Stadskamrerare L. Vogel; Sekreterare L. Gräslund.
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Daily Newspaper <i>Morgentidningen</i> , Stockholm.	Herr Müller, Representative.
Daily Newspaper <i>Dagens Nyheter</i> , Stockholm.	Herr Samuelson, Representative.

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## Chapter I

### PUBLIC ADMINISTRATION IN SWEDEN

#### CENTRAL

SWEDEN is an ancient country. The Kingdom of the Sveas was centred round old Uppsala where heathen ceremonies and sacrifices to the old Nordic gods took place. The Swedish name *Sverige* means the kingdom of the Sveas.

In 1435 King Engelbrekt called a Parliament embracing the whole nation with the four estates—nobles, clergy, burghers and peasants. The Parliament of the four estates continued until 1866, when a two chamber system was adopted: the upper house elected by the councils of counties and cities and the lower house by universal suffrage.

The present Bernadotte dynasty was founded in 1810 by the election of Jean-Baptiste, Marshal of France, to the vacant Swedish throne. Sweden is a limited monarchy, although according to the constitution the King has the sole power to govern. Each week the King sits in council with the cabinet, consisting of the ministers in control of departments of state (*statsråd*) and other ministers without portfolio (*konsultativa statsråd*). All decisions are decisions of the King and all must be signed by him, but none is legal without the signature of the appropriate minister of state. The minister is responsible for his acts, but the King cannot be held in question and he makes no decision which is not approved by the cabinet. In Sweden the principle of parliamentary supremacy has long been accepted.

The civil administration is supervised by the government through the departments of state—Justice, Foreign Affairs, Defence, Social Welfare, Education, Commerce, Agriculture, Finance, etc. The actual administration is conducted by central boards (*centrala ämbetsverk*), which enjoy a freedom from ministerial control regarded as a unique feature of Swedish public administration. In 1720 Parliament enacted that cabinet ministers should not head the central administrative boards. Each central board has its letter of instruction from the Crown, defining its authority and duties, and while coming under supervisory oversight by a department of state, it is subject only to the cabinet as a whole.

There are several state enterprises (*affärsdrivande verk*) operating such services as the railways and post office.

The local government system (*lantregeringen*) comes under the jurisdiction of the Ministry of the Interior (*Inrikes-departement*).

#### PROVINCIAL

A feature of public administration in Sweden with no counterpart in the United Kingdom is the system of provincial government (*länsstyrelse*) on behalf of the Crown by governors (*landshövding*), whose jurisdiction embraces the whole area of a province (*län*). There are twenty-four provinces with the old historic boundaries and the special province of Stockholm, where the governor is given the title of governor-general (*överståthållare*).

The first governor—the guardian of the peace and King's agent—was appointed by the King in 1634. The governor is still the Crown's representative appointed by the King-in-council, but his authority is now derived from the Ministry of the Interior. The Crown directive defining the duties of governor requires him to "give attention to the condition and needs of the province, to seek in all things to further the prosperity of the province and the welfare of the people, to keep the Crown informed on all matters of importance concerning the province and its people and to make recommendations to the Crown where actions are required which are beyond his authority."

The governor has supervisory powers over local authorities and takes a hand in the administration of local services. It is his responsibility to satisfy himself that the local authorities discharge their duties properly. The minutes of the proceedings of the local authorities are sent to him. He has the right to be present at local council meetings and to take part in the debates, but not to vote. On his staff are the provincial chief of police (*landsfogden*), who controls the communal and state police, the district police chiefs (*landsfiskaler*), who act also as district prosecutors, the director of civil defence (*civilförsvarsinspektör*), the provincial fire inspector (*länsbrandsinspektör*), and other officers engaged in local services. His office carries out important executive functions, among which are the registration of persons and the supervision of income taxes, communal and national.

Any citizen who considers that an act of a commune is *ultra vires*, infringes his rights, or is otherwise not well founded, may complain to the governor. If not satisfied with the governor's ruling, the complaining citizen or the council of the commune may then go to the courts. Where the governor has reason to believe that a commune is

not discharging a duty as required by statutory regulations, he may order it to do so. In such a case the commune may appeal to the courts to have the governor's order set aside or modified.

The officers of the provincial governor also play an important part in Swedish local government in both its functional and financial aspects. The two chief officers are the provincial treasurer (*landskamrerare*) and the provincial secretary (*landssekreterare*).



## Chapter 2

### LOCAL GOVERNMENT IN SWEDEN

#### THE STRUCTURE AND LEGAL BASIS OF LOCAL GOVERNMENT

IN Sweden the tradition of local affairs being managed by local people goes far back into its history. Local government took shape in pagan times. When Christianity came to the north, the country was divided into parishes (*socken*) for the management of local ecclesiastical and secular affairs, an arrangement which continued into modern times. The requirements of social evolution and economic development rendered the parish meetings no longer suitable for the needs of the country, and in the middle of the nineteenth century the system, which had survived for several centuries, was brought to an end.

The communal law of 1862 separated civil and religious affairs. A commune (*kommun*) was created to administer civil matters and a church meeting (*församling*) was set up to deal with ecclesiastical affairs. This law also established the county councils (*landsting*) for dealing with services beyond the resources of the smaller communes. Their boundaries coincide with those of the provinces, the areas of administration of the provincial governors.

In medieval times, parish government soon became inadequate for the growing towns, and rights and privileges were granted to them by charters from their overlords. Town councils were elected by the burgesses. The six largest cities in Sweden—Stockholm, Göteborg, Malmö, Norrköping, Helsingborg and Gävle—do not come under a county council. They discharge county council services and are autonomous authorities for local government purposes. These six cities are the county boroughs of Sweden.

In 1862 there were 2,300 rural communes, most with populations under 2,000. Communities so small could not cope with the growth of government which has taken place since then. A year or two ago a major re-organisation of the areas of local government was undertaken, and to-day in Sweden there are 814 rural communes. The following are the local government bodies in existence at the present time:

Cities ( <i>städer</i> )	133
Market towns ( <i>köpingar</i> )	90
Rural communes ( <i>landskommuner</i> )	814
County councils ( <i>landsting</i> )	25

Outside the six cities referred to above, there is a two-tier system of local government, with primary local authorities (*primära lokala myndigheter*), namely the rural and urban communes; and secondary local authorities (*sekundäre lokala myndigheter*), namely the county councils. The county councils have their own defined duties and services which they discharge over the whole of their area with the exception of the six cities, and they do not administer any of the services of the primary local authorities. In a number of the more populous rural areas, where market town status has not yet been attained, a municipium may be constituted to perform services which are provided in the market towns. The municipium is regulated by a municipal council (*municipalsamhälle*). There are 180 such bodies.

Local authorities are composed of councillors elected every four years. They discharge their corporate functions by reference and delegation to committees. There is no city manager system. In Stockholm there are 100 members—the 100 tyrants as they are called.

The committees are the framework of the administrative organisation, and it is they which conduct the business of the local authority. Only the council can approve the annual budget, authorise expenditure not contained in the budget, borrow money, purchase or sell land, and fix the communal income tax. By this means the council holds in its own hands the reins of financial control.

Each local authority must appoint a central committee, which acts as the executive board of the council. This is regarded as the local "cabinet" and is the real seat of power in communal administration. It exercises a general authority over all the other committees, although it cannot interfere with the ordinary administration of these committees where their acts are in accordance with statutory regulations. By special statutes there are several committees which must be appointed, e.g., Education, Health, Child Care, Public Assistance and Town Planning, and the council itself can neither curtail nor extend the duties of these committees. Nevertheless, in the last resort, the council and the central executive committee have the power of financial control.

The central committee also acts as the finance committee and it is concerned with the management of communal property, the preparation of the budget, recommendations for the communal tax, collection of revenue, and the general superintendence of financial affairs.

How the central committee works is well exemplified in Stockholm. Between the city council and the executive committees stands the city collegium or central board of administration (*stads kollegium*). This consists of twelve councillors, reflecting the strengths of the political



parties, and it is regarded as the "cabinet" of the city council. It meets each week to transact its business. All new proposals from committees and departments must come first to the collegium, which prepares all matters submitted to the city council and directs the city administration. The financial secretary (*finans sekreterare*) works directly under the collegium.

The different kinds of local authorities are combined into associations—the union of rural authorities (*landskommunernasförbundet*), the union of cities (*stadsförbundet*) and the union of county councils (*landstingsförbundet*).

What are called the communal laws contain the provisions relating to such matters as the election of councillors, constitution and procedure of local authorities, their accounts and expenses, borrowing, the preparation of an annual budget, and the power to impose local taxes. Each kind of commune has its own communal law, and there are no local or private statutes. There is a separate body of communal laws applicable to Stockholm. The communal laws were consolidated in 1862, when local government was re-organised. They were amended and extended repeatedly until 1930 when they were re-enacted. The communal laws of 1930 are the present basis of the organisation of local government in Sweden.

The principle of "self government" (*själv styrelse*) is carried much further in Sweden than in the United Kingdom, and this is responsible for many of the differences which exist between the institutional structures of the two countries. "The people are to govern themselves": the application of this principle is seen in the elected boards which assess income for tax purposes, and in the appointment of town councillors to executive positions in the Stockholm administration. The local assessment boards are dealt with elsewhere in this report. The administrative structure in Stockholm is described briefly below.

The municipal administration of Stockholm is divided into a series of departments, e.g., Finance, Personnel, Property, Industrial, Health and Welfare. At the head of each is a commissioner (*borgarråd*) who is elected by the city council from their own number for the period of four years (the life of the council) and who is responsible for the administration of his department. The commissioners are political representatives of the parties and are official representatives of the municipal administration. Customarily they sit as chairmen of one or two of the committees attached to their departments. Together the commissioners compose a special committee, with the commissioner for finance, by virtue of his office, acting as chairman. It is their duty to impart co-ordination and planning into the management of the



affairs of the city council. Most, if not all, new proposals for the city council originate in the commissioners' committee, from which they go as recommendations to the city collegium, whose sessions the commissioners are required to attend. They receive salaries comparable with those of cabinet ministers, and are awarded pensions when their offices terminate.

#### FUNCTIONS OF LOCAL GOVERNMENT

The functions for which local authorities are responsible are similar in Sweden and the United Kingdom, with the important exceptions of hospitals which are a local service in Sweden and secondary education which in Sweden is a state function.

The general communal law relating to primary communes, rural and urban, confers wide powers of self-government on the communal councils. It provides that "the commune shall maintain public order and administer its domestic affairs in so far as authority over these matters has not been conferred by law upon another." A commune cannot encroach upon the functions of the national government, the provincial governors and other national bodies. The communes are empowered "to look after the interests of the community." There is no explicit definition of these general powers, and how far local authorities may extend their activities by virtue of these powers is an open question. A local authority may undertake almost anything it chooses so long as it does not encroach on the authority of another body, and so long as the proposed undertaking is for the furtherance of the public welfare within the commune. The powers cannot be used to support private industry, although this prohibition does not operate to prevent local authorities carrying on undertakings which are of the character of private enterprises, e.g., tramways, gas works, power stations. In Stockholm the transport undertaking is run by a company whose shares are owned by the city council. The city council also owns shares in the company which runs the largest hotel, "Malmen," in Stockholm. Since these powers are to be exercised for the public welfare, local communes may not, under the general communal law, use their funds for the benefit of private individuals or sectional groups. They may, however, operate baths and wash-houses and provide parks and sports grounds, which are available to the whole population. County councils, which are comparative newcomers, do not have these unspecified general enabling powers.

. As already stated, any citizen who considers a decision of the communal council contrary to law or ill founded, may seek redress by a

complaint to the provincial governor and, from him, to the courts. In this way precedents have been established which serve to set the nature and limits of the ancient communal law powers of the communes.

Local authorities are also responsible under special statutes for particular services such as child care, elementary education, and public assistance.

The county councils have limited functions. The most important is the hospital service to which are allied certain health services, such as dentistry, midwifery, district nursing and care of expectant and nursing mothers. The county councils provide also certain types of education—vocational and occupational training and adult education in people's high schools (*folkhögskolor*). They run children's homes. The six largest cities provide these county council services themselves. The county councils do not administer any of the services for which the primary communes are responsible, but there are sometimes transactions between them, e.g., contributions for chronic sick cases in old people's homes and for home helps where there is an element of liability on the county council as the hospital authority. There may also be contributions where a primary commune has been permitted to undertake vocational education.

The primary communes provide services similar to those provided by local authorities in the United Kingdom—police, fire brigades, road and parks, planning, housing, civil defence, public hygiene and water-works, sewers, cleansing, food hygiene, education, social welfare, including public assistance, child care, and social insurance and health services. In addition there are public utility undertakings such as gas, electricity, trams and buses, and harbours.

In the local government statistics published by the Central Statistical Bureau (*Statistiska Centralbyrån*), there appear income and expenditure for church purposes. Church administration is based upon the parishes (*församlingar*), with the groups of parishes in the primary communes being regulated by a church council (*kyrkofullmäktige*). The church council prepares an annual budget and the deficiency is met by means of an addition to the communal income tax, which is thus in two parts, one for the commune (*borgerlig kommun*) and the other for the church (*kyrklig kommun*). The produce of the combined tax is received by the commune from the provincial governor's office (*länsstyrelse*), and the commune hands over to the church council the part which is attributable to the church tax supplement. In 1951 in Malmö the communal tax was 8.53 and the church tax .47, making a total tax of 9.00 per kr. 100 (per *skattekrona*).

Local authorities administer old-age pensions and family allowances



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on behalf of the government, which meets the cost. They are empowered to grant supplementary pensions to those in need, but only out of their own funds.

Over the years Sweden has developed a system of social welfare comparable with that of the United Kingdom. In 1953, a bill was passed by Parliament to establish a unified and comprehensive scheme of health and social insurance covering the whole population. The new scheme is financed by contributions from the insured persons, employers and the state. The law came into operation on 1st January, 1955. Previously sickness and unemployment insurances were not compulsory, having been administered on a voluntary basis by approved societies acting under the supervision of a government agency with financial assistance from the state. Unemployment insurance was undertaken by trade unions. Contributions were paid by the participating persons to the funds of these voluntary agencies. As from 1st January, 1955, these funds were taken over by the state.

In 1954 the old-age pension, including the cost of living supplement, was kr. 1,750 for a single person, with an addition of kr. 1,050 for a wife. It is payable at the age of sixty-seven. The family allowance is kr. 290 for each child under sixteen years of age. This allowance is not taxable, and no deduction is made for children in computing either the national or the communal income tax.

### FINANCE OF LOCAL GOVERNMENT

The Finance Committee is charged with the duty of preparing each year a budget for the ensuing financial year for submission to the council of the commune. Only the council has power to authorise expenditure appropriations and to fix the local tax. There is no requirement that the budget, after approval by the council, be submitted to any higher authority, but government authority is required for projects involving the payment of exchequer grants, the Government Accounting Office (*Riksräkenskapsverket*) must be satisfied that state grants have not been misapplied, and loans with repayment periods of more than five years may be raised only with the sanction of the Department of Finance (*Kungliga Finansdepartement*).

The procedure for the compilation of the budget follows the same lines as in the United Kingdom. Departments and committees for the various services prepare their figures and forward them to the Finance Committee. The collated estimates are presented to the full council along with the report and recommendations of the Finance Committee.

Local authorities have power to establish reserve funds and may contribute such sums as they think fit to such funds. The most notable



is the Tax Regulation Fund (*Skatteregleringsfond*). This plays an important part in the finance of local government in Sweden. On occasions the government has directed local authorities to contribute sums to these Tax Regulation Funds. This was done in 1953 and 1954, probably having in mind the high level of employment and the possibility some day of a recession taking place. No more than one-third of the fund may be withdrawn in any one year without the consent of the government. Other funds, such as capital and insurance funds, may be created. No maxima are prescribed for these funds. In 1951 the total of the Tax Regulation Funds for all local authorities amounted to kr. 359 millions, and of other funds to kr. 807 millions.

Local authorities may invest in business enterprises within the powers conferred upon them by the ancient and somewhat ill-defined communal law. Stockholm, more than any other local authority, has taken advantage of this power, having acquired part ownership of fifteen joint stock companies rendering services or conducting business of a nature in which the municipality has a special interest. In some of these companies, the private shareholding does not have real significance and the appointment of board members and executive is in the hands of the city council. Among these companies are the Stockholm Transport Company, Stockholm Leasehold Company, Stockholm Homes Company and the Swedish Housing Company.

To some extent capital expenditure is defrayed out of ordinary revenue. In 1951 expenditure in the cities on acquisition of real estate and property and new construction amounted to kr. 492 millions, and borrowings for that year amounted to kr. 426 millions. In the market towns the expenditure was kr. 42 millions and loans totalled kr. 24 millions. In the rural communes, where the disparity is much greater, the expenditure was kr. 206 millions and loans were kr. 85 millions.

Having approved the estimates, the next step is for the council of the commune to fix the rate of the communal income tax.

The local financial year is the calendar year, and this is the fiscal year for the income tax, national and communal. Towards the end of the year, the rate of the communal income tax is fixed for the ensuing year. The determination of the rate requires careful consideration, because its basis is more variable than the United Kingdom one of the annual value of land and buildings. Estimating the yield of the local income tax gives rise to much the same problems as estimating that of the national income tax in the United Kingdom, although in Sweden the difficulties are somewhat greater as all income, including trading profits, is assessed on the current year's basis, while in the United Kingdom profits are assessed on the previous year's

basis. The estimates are made by the commune finance officer in conjunction with the tax officers of the Crown. The usual procedure is to start with the known assessed income of the previous year, which is notified to the commune by the tax charge office, and then to estimate the current year's income mainly by reference to the preliminary payments of tax made during the year; this figure is then projected forward to arrive at an estimate of the chargeable income for the coming year. To enable this to be done, investigations are made into the trend of trading conditions and of wage and salary movements, and large companies are asked to forecast the trend of their profits for the coming year. Stockholm City Council has a statistical section whose duties include enquiries and investigations for the purpose of arriving at an estimate of the taxable income of the budget year. Other local authorities do not employ staffs of statisticians, but their problem is not so great.

It was claimed that estimating taxable income was facilitated by the fact that 85 per cent of the income tax comes from personal incomes and only 15 per cent from corporate bodies, percentages quite different from those in the United Kingdom. The contention rests on the proposition that personal incomes, mostly salaries and wages, are less difficult to estimate than corporate incomes, mostly business profits. The argument must, however, be accepted with some reserve. Because of the onerous tax position of companies, this form of business enterprise has not been so widely used as it is in the United Kingdom, where many family businesses have been transformed into private companies. A considerable part of the income tax from personal incomes comes, therefore, from trading profits of private concerns, and these can be as difficult to estimate as profits from companies.

The differences in the percentages may also be partly due to the fact that Sweden is not so industrialised as the United Kingdom. Of the total Swedish population of 7,044,000 in 1950, the working population was 3,120,000 or 44 per cent, excluding housewives. Agriculture, forestry and fishing accounted for 21 per cent; and industry, including mining, for 41 per cent. There are only three cities with populations exceeding 100,000—Stockholm, Göteborg and Malmö. In the rural communes there is little manufacturing. In few of the smaller towns are there large industrial enterprises. In some towns the whole economy depends on one large undertaking. In Sandviken, which has a population of 20,000, the life of the whole community depends upon the ironworks. Outside the larger cities, therefore, the difficulty of estimating taxable income is not so formidable and the system works smoothly.



That it does so, is due in large measure to the steady progress of trade and freedom from recession during the years since the end of the war, and to the very conservative estimates made of taxable income. The tax revenue paid to the communes during the financial year is the yield of the preliminary tax, and usually there are large balances to be paid in the following year when the final tax is computed. Local authorities have therefore a hidden reserve of tax income to come in in the future. In the Uppsala budget for 1954, out of the total communal tax income put at kr. 25,361,000, balances on 1953 account amount to kr. 5,441,000.

Since the end of the war there has been inflation in Sweden as well as in the United Kingdom, and this is reflected in rising money incomes and increased tax yields. This trend is not regarded as of vital importance, because inflation affects equally the expenditure side of the communal financial accounts. Conservative estimating of the taxable revenues, with a balance up one's sleeve, seems to be the general rule. Vagaries in trading conditions would cause fluctuations in the rates of tax, and the steadiness of the rates over the past years is an index of the post-war stability in the economy of Sweden.

In this connection the tax regulation funds (*skatteregleringsfonder*) are important and, during the good years since the war, the government has instructed local authorities to contribute to these funds. At the end of 1951 they amounted to kr. 359 millions and they have grown since. This is a considerable sum for a country with a population of 7,150,000. On a similar basis the figure for the United Kingdom would be of the order of £170 millions. The purpose of these funds is not only to even out tax rates from year to year. They are also intended to provide funds to draw upon should a recession occur.

Communes do not have equal taxable resources. There are areas with low incomes per head, especially sparsely populated rural areas of poor fertility and little timber. Tax Mitigation Exchequer Grant (*skattelindringsbidrag*) is paid to such communes. A high rate of communal income tax may be due both to a low income per head and a high expenditure per head. Both those factors are taken into account in calculating the Tax Mitigation Exchequer Grant.

The council having fixed the rate of tax to be levied, the rate is then intimated to the provincial governor's office, which sets in motion the national tax organisation.

At intervals of two months, the provincial governor pays over to each commune instalments on account of the communal income tax, based on the budgeted yield from the rate of tax fixed. When eventually the final tax (*slutlig skatt*) for the financial year is assessed, the



## LOCAL GOVERNMENT IN SWEDEN

balance due to the local authority is remitted to it by the provincial governor. Nearly always considerable balances of final tax are paid over at the end of the financial year.

The local authorities receive the gross yield of the tax with no deduction for bad debts or cost of collection. In the thirty cities where the tax charge office (*uppbördsverket*) is owned and operated by the town council, this cost is borne by the local authority subject to a contribution from the Exchequer.

### THE UPPSALA CITY BUDGET FOR 1954

A summary of the Uppsala City Council budget for 1954 is included as Appendix I, Table 5. Uppsala, a university town and the ancient capital of the Sveas, has a population of 66,000. The gross estimated expenditure, revenue and capital, amounted to kr. 42,104,000, from which were deducted in the first instance receipts from rents, charges, dues and so on, amounting to kr. 6,680,000, and income from exchequer grants put at kr. 5,607,000, leaving a net expenditure of kr. 29,817,000. This sum includes a contribution to the Tax Equalisation Fund (*Skatteutjämningsfond*) and also contributions to various special funds. A sum was provided for contingencies or unforeseen expenses.

Capital expenditure was estimated at kr. 2,478,000, none of which was borrowed. Special receipts, mostly from the sale of land, applied towards capital expenditure were estimated at kr. 922,000. Revenue contributions of kr. 887,000, described in the budget as capital income of the tax account, consist mainly of charges to revenue expenditure for the depreciation of capital assets. The balance of capital expenditures, amounting to kr. 669,000, was also met out of the local tax yield.

A surplus of kr. 526,000 from the gas and electricity undertakings was applied in relief of the local tax, and also an income of kr. 1,868,000 from income from investments of funds and fixed assets, leaving kr. 25,614,000 to be raised by means of local taxation. The minor local taxes—dog tax, artistes tax, and the proportion of the entertainment tax retained by the city council—were estimated at kr. 323,000, leaving kr. 25,291,000 to be met by the communal income tax. In relation to the tax yield, the surplus taken in from the utility undertakings is negligible and, of the local taxes, the minor taxes are insignificant compared with the communal income tax. Capital receipts (sales of land, etc.) amounted to kr. 922,000, and revenue appropriations for depreciation of capital assets to kr. 887,130. Of the total local tax income of kr. 25,614,000, income tax accounts for 98.7 per cent and minor taxes only 1.3 per cent.

Taking exchequer grants and local taxes together, amounting to kr. 31,221,000, as the total tax-borne municipal expenditure in Uppsala for 1954, national taxpayers met 18 per cent and local taxpayers 82 per cent.

#### ANALYSIS OF LOCAL AUTHORITY EXPENDITURE AND INCOME

Statistics of local authority expenditure and income are given in Appendix I, Tables 2, 3 and 4. These have been taken from the local government publications for 1951, issued in 1953 by the Swedish Central Statistical Bureau (*Sveriges Statistiska Centralbyrån*), in Stockholm.

The gas and electricity industries have not been nationalised in Sweden. An important question is the extent, if any, to which profits from such municipal enterprises are appropriated in relief of local taxation. In 1951 the total expenditure, revenue and capital, amounted to kr. 411 millions against revenue of kr. 422 millions, leaving an overall surplus of kr. 11 millions. During the same year capital outlay amounted to kr. 90 millions, but unfortunately the statistics do not show how much of the capital outlay was met out of loans and how much out of revenue. Had it been met wholly out of loans, kr. 100 millions would have been available for taxation relief purposes. It is likely, however that the profits actually appropriated were considerably less. In any event it is clear that, by comparison with the total of kr. 2,579 millions raised by local taxes and exchequer grants, trading profits are not of great importance in Swedish local finance.

In discussion about the use of public utility profits for general revenue purposes, the Financial Secretary of Stockholm City Council said that in Sweden local authorities were not permitted to impose indirect taxation, and he expressed the view that, having regard to this prohibition, local authorities cannot, at least overtly, frame budgets in such a way as to reduce taxes by means of revenue surpluses on trading departments. However, as the Uppsala budget discloses, such profits are in fact taken into account, but they are not large enough to have any significant effect on the rates of local income tax which have to be levied.

The total expenditure of all local authorities in 1951 was kr. 4,573 millions, and income was kr. 4,461 millions, leaving an apparent deficiency of kr. 112 millions. No explanation of this is given in the statistical publications. It may have consisted of deficiencies carried forward to 1952, or it may have been met by withdrawals from tax regulation or other funds. The apparent deficit is not of great importance in relation to the total figures involved.

Excluding the public utilities and borrowings, aggregate income of



#### LOCAL GOVERNMENT IN SWEDEN

local authorities in 1951 amounted to kr. 3,359 millions, of which specific receipts made up kr. 780 millions, exchequer grants kr. 598 millions, and local taxes kr. 1,981 millions. Local government expenditure was therefore met to the extent of 76.8 per cent out of taxes, national and local.

Of the tax-borne expenditure in 1951, subventions from national funds met about one-quarter and local taxes three-quarters. In the United Kingdom the tax-borne expenditure of local government in 1951-52 was met almost equally by national taxes and local rates. Both countries make use of the system of exchequer grants in aid, but considerably less in Sweden than in the United Kingdom. Local authorities in Sweden are less likely, therefore, to be under the control of the central departments.



## Chapter 3

### THE INCOME TAX ADMINISTRATION IN SWEDEN

For both communal and national income tax, the system for the assessment of income, the calculation of tax payable, the issue of demand notices and the collection of tax, is the same. The administration of the two income taxes is wholly integrated in the one organisation.

#### ASSESSMENT OF INCOME

Each province (*län*) is divided into assessment districts. There are two kinds of district. For the assessment of private persons, the province is divided into local assessment districts (*lokala taxerings-distrikt*), each one consisting of a commune or part of a commune. For the assessment of the remaining taxpayers—companies and other bodies—the assessment district is the province itself (*särskilt taxerings-distrikt*). The office of the provincial government (*länsstyrelse*) determines the delimitation of the districts.

For each local assessment district, a local assessment board is appointed (*lokal taxeringsnämnd*). The chairman and another member, the Crown representative (*keronombud*), are appointed by the provincial governor. The other members are appointed by the communal council. If a commune is divided into two or more local assessment districts, the provincial governor may order that certain groups of taxpayers shall be dealt with by a special board (*speciell taxeringsnämnd*) rather than by the local boards within whose areas they reside. This power has been exercised to an increasing extent during the last few years in order to secure more uniform assessment of taxpayers such as commercial travellers, doctors, dentists and lawyers.

The chairman of each provincial assessment board and the Crown representative are appointed by the provincial governor, and the other members are appointed by the county council and by the town council of any city within the province which does not come under the county council.

In Stockholm there is a special assessment board (*gemensam taxeringsnämnd*) for dealing with taxpayers not resident in Sweden.

Sweden is thus covered with a pattern of assessment boards, which are responsible for the assessment of all income liable to tax, and it is

## THE INCOME TAX ADMINISTRATION IN SWEDEN

to them that every person is under a duty to submit a declaration of income. The forms are obtained from public offices, and the completed returns, showing the income of the previous calendar year, which is the tax year, are required to be forwarded to the assessment boards in the month of February each year. There are about 2,500 assessment boards in Sweden. In Stockholm there are 140 boards. In Uppsala, which has a population of 66,000, there are 30 boards.

None of the members of these numerous boards, which are appointed annually, is a paid official. They are private persons and unpaid. In practice they are selected because of their knowledge and experience of public affairs and their occupational suitability. Frequently the chairman or Crown representative is a member of the provincial governor's staff. For groups of assessment boards, a *taxeringskonsulent* is appointed by the provincial governor to assist the boards in dealing with the more complicated cases. The *taxeringskonsulent* is not a paid tax official, but a private person like the members of the boards.

In 1951 a national tax board (*Riksskattenämnden*) covering the whole kingdom was set up in Stockholm, with the duty of giving advice and directions to assessment boards and appeal boards, in order to promote proper application of the tax laws and practice. Taxpayers also are entitled to consult the national tax board in certain kinds of cases. They may for example, before transactions are completed, ascertain from the board what would be the taxation consequences of the results of those transactions. The taxpayer must go to the national tax board before the question is dealt with by the assessment board. Decisions of the national tax board can be reported for the views of the Supreme Court (*Regeringsrätt*). The provincial tax superintendent can take decisions of the national tax board to the Supreme Court only on questions of fact, not of law.

A leading practising chartered accountant in Stockholm expressed the view that the national tax board has already proved very useful to business men and accountants.

A firm of advocates in Stockholm said the board is a very useful institution. Tax questions on transactions in prospect can be settled quickly. The ordinary machinery of appeal takes much longer if the case goes through all the stages to the Supreme Court. The board members are appointed by the Crown.

The supervision of the work of taxation in each province rests upon the provincial governor's office (*länsstyrelsen*), which is divided into two main departments, one for general administration and the other for finance. The provincial governor also appoints the chairmen of the assessment boards, and the *kronoombund* and *taxeringskonsulenter*.



Within the financial department is a taxation section (*skatteavdelning*) in charge of a taxation superintendent (*taxeringsintendent*), to whom the assessment boards within the province send the lists of taxpayers and the amounts of their assessed incomes. In fact the assessment boards send the lists to the provincial governor, in whose office two copies are made, one being handed to the tax superintendent who is concerned only with the correctness of the assessed income, and the other to a tax charge office (*uppbördsverket*) where the amounts of tax payable are calculated and the demand notes are issued.

It is the duty of the tax superintendent to examine the lists and to satisfy himself that they are correct. If he is not satisfied, the tax superintendent has power to call for books and papers and to examine the books of account with the help of an accounts investigation section (*bokgranskningssektion*) in his office. He may go to the appeal board (*länsprövningsnämnd*) and appear before the board on behalf of the Crown. When a case is taken to the appeal board, the papers from both the tax superintendent and the taxpayer go to the provincial treasurer (*landskamrerare*) or, in Stockholm, the financial director (*skattedirektör*), who is the chairman of the appeal board. Both the chairman of the board and the tax superintendent, who appears before him, are officials of the provincial governor's office (*länsstyrelsen*). The provincial tax superintendent is the official whose duties most nearly approach those of the inspector of taxes in the United Kingdom.

An appeal board is appointed for each province (*prövningsnämnd*). The provincial treasurer (*landskamrerare*) or, in Stockholm, the financial director (*skattedirektör*) is chairman *ex officio* of the appeal board. The other members are appointed by the Crown.

Appeals may be made to these boards by taxpayers, communes and also by the provincial tax superintendent, and they have power to vary the decisions of the assessment boards. The boards have power also to issue directions and advice to the assessment boards.

For dealing with taxpayers who have income arising in more than one province, there is an intercommunal appeal board (*mellankommunalprövningsnämnd*) in Stockholm. It functions along with the provincial appeal boards and is concerned mostly with questions raised by communes as to the allocation of assessed income between the various communes in which the income arises, e.g., in the case of companies with establishments in different parts of Sweden. The board members are appointed by the Crown.

Decisions of the appeal boards may be taken to the Court of Exchequer (*Kammarrätten*) both on questions of law and fact. This is the central administrative court for taxation matters. Its decisions are



## THE INCOME TAX ADMINISTRATION IN SWEDEN

final only on questions of fact concerning the valuation of real estate.

Finally, decisions of the Court of Exchequer, subject to the exception mentioned, may be taken to appeal to the Supreme Court (*Regeringsrätten*)

All tax appeals are free of court costs.

### COMPUTATION AND COLLECTION OF TAX

Throughout Sweden there are tax charge offices (*uppbördsverk*) where the income taxes, communal and national, are computed. During the tax year payments are made on a preliminary estimate (*preliminär skatt*) and, when the assessments for the year are received from the assessment boards, the proper amount of tax payable is calculated and assessment notices, showing tax under- or over-paid, are prepared and issued.

There is a tax charge office in each of the large towns, where the official in charge is called the Crown accountant (*kronokamrerare*). Elsewhere the communes are combined under one office, where the official is called the district registrar (*häradskrivare*). Altogether there are about 180 tax charge offices in Sweden. In thirty of the largest cities and towns the offices and officials are provided and paid by the commune, and in other places they come directly under the state.

The preliminary tax payments made during the year are calculated at the rates fixed at the end of the previous year by the communes and the government.

In the case of salary and wage earners, deductions are made by the employers according to tax tables and accounted for by the employers. In the case of profits, the preliminary tax is calculated on estimates of the profits. To discourage the under-estimating of profits in order to reduce preliminary tax payments, penalties are imposed on arrears. The penalties apply to all taxpayers and are chargeable where the arrears are more than kr. 1,000. The penalty is 5 per cent on the amounts of the arrears over kr. 1,000. If a balance is due by the Crown, it is repaid to the taxpayer with an allowance of 3 per cent.

The income tax calendar for the year 1954 is as follows:

Declaration of income for 1954 by taxpayers to assessment boards	February, 1955
Assessment of income by assessment boards	February to June, 1955
Submission of lists of taxpayers and assessments by assessment boards to provincial governors	June, 1955

## THE FINANCE OF LOCAL GOVERNMENT IN SWEDEN

Issue of notices of assessment and final tax payable	November and December, 1955
Repayment of tax overpaid	November and December, 1955
Payment of tax underpaid	January to April, 1956

The tables used by employers for the deduction of income taxes from salaries and wages are less complicated than those in use in the United Kingdom. There are only two personal allowances, one for single persons and the other for married persons. No allowances are granted for children, but the family allowances paid to mothers are not subject to income tax. An additional allowance is given to a married woman who has income. The tax tables provide for four classes of taxpayer: a married man whose wife has no income; a married man whose wife has income; a married women or single person with child or children; a married woman or single person without child or children.

The tax deductions are on a non-cumulative basis. They are determined by the amount of the weekly wage or monthly salary, each week or month standing on its own with no carry-forward from previous weeks or months. This simplifies the tables and obviates difficulties when an employee changes his employment.

The tax charge offices send copies of the final tax assessment notices, all of which are coded to identify the taxpayers, to the tax department of the general post office (*postverketskatteavdelningen*) in the town in which the provincial governor's office is situated. Payments of tax by employers for employees and by other taxpayers are made to banks and post offices, which transmit the moneys to the general post office. There the personal accounts of the taxpayers are kept. The moneys are then paid over to the provincial governor's office and from there to the Riksbank on account of the Crown (*Statskontor*).

It is the tax charge office which works out for each commune the total taxable income of the commune for communal income tax and calculates the amount of the tax yield to be paid to each commune.

With communal income tax the residence of the taxpayer is of cardinal importance, because it is residence which fixes the commune to which the communal income tax is paid. When an individual moves no attempt is made to allocate his tax to the different communes in which he has resided. The taxpayer's residence is fixed for the whole of the tax year. All persons are registered on 1st November each year, and it is the residence on that date which determines the commune to which the communal tax for the following year is paid. The registration, which is used also for elections, is carried out by the

## THE INCOME TAX ADMINISTRATION IN SWEDEN

tax charge office (*upphörsverket*). In Stockholm there is a special registration office called the *mantalsverket*.

The registration office prepares lists for each commune in its area and divides these lists into the assessment districts. Lists are forwarded to the assessment boards which subsequently enter the assessed incomes of the taxpayers. The completed lists are then sent by the boards to the provincial governor's office, where two copies are made, one for the provincial tax superintendent (*taxeringsintendent*) and the other for the tax charge office.



## Chapter 4

### THE MAIN FEATURES OF THE SWEDISH COMMUNAL INCOME AND PROPERTY TAXES AND OF THE NATIONAL TAXES ON INCOME AND CAPITAL WHICH AFFECT LOCAL TAXATION

IN general the principles governing the division of income into categories and the methods of computing profits, income, and property for the Swedish communal taxes are adopted in the State Income Tax Law. The interaction of the communal and state taxes, which are normally assessed and collected concurrently, is important and is described more fully in Chapter 7. The principal law is the one governing the communal income and property taxes. It is this law which contains the definitions of chargeable income and property, of residence, year of assessment, tax year, certain deductions and other matters common to both communal and national taxes. The law imposing the national taxes adopts these provisions of the Communal Tax Law by reference to the relevant articles and is by contrast much briefer.

#### COMMUNAL INCOME TAX

The rates of communal income tax are fixed by the commune in which the taxpayer resides. The income to be taxed in the commune of residence is the whole of the income of the resident which is not localised in accordance with the statute in some other commune. Income which is charged otherwise than in the commune of residence is chargeable as follows:

- (a) Income from agricultural or other real property is assessed in the commune where it is located;
- (b) Income from trade or business is assessed wherever there is a permanent establishment;
- (c) Profits from the resale of real property are charged where the property is situated;
- (d) Income taxable under Swedish law which has been earned or received in respect of a period of non-residence in Sweden is assessed in Stockholm for combined communal purposes.

## THE MAIN FEATURES OF THE SWEDISH INCOME TAXES

The fact that income from trade or business is assessed wherever there is a permanent establishment means that where there is more than one permanent establishment the income must be apportioned between them. We were informed at the outset that this was one of the main problems of Swedish taxation of business profits. The matter is of considerable importance and is discussed at length in Chapter 8. Where there is no permanent establishment in the commune, that commune has no power to tax.

From 1st January 1955, the property tax has been merged to form part of the income tax. The property tax was previously charged under the provisions of Sections 4 to 16 of the Communal Tax Law. It formed, in law, a separate tax, but it was administered through the same machinery as the income tax and occupied in relation to that tax a position similar in many respects to that which Schedule A occupies in relation to other income charged with income tax in the United Kingdom.

The change converts the annual value of property into income chargeable with income tax, subject to a proviso that the annual value shall not be less than 4 per cent of the assessed capital value of the property. The main purpose of the change is to permit personal allowances to be set against property tax; this was not possible under the old law. The reservation regarding the 4 per cent minimum value is to protect the commune against loss of revenue which might arise from substituting the actual income from a property for the notional basis which previously obtained. If a property produces more than 4 per cent of the assessed capital value, the yield is charged with tax. In 1953 property tax accounted for one-ninth of the total assessment of income and property tax.

The communal income tax conforms to the schedular type, the divisions being:

- (a) Agricultural property;
- (b) Other real property;
- (c) Trades, businesses and professions;
- (d) Employments;
- (e) Casual sources including capital gains;
- (f) Income from invested capital.

Category (e) includes profits from the disposal of movable and immovable property, and from lotteries. Category (f) includes both income from capital invested in Sweden and income from property

and businesses abroad. Losses are only available for set-off against income within the same category.

The rules regarding computation of income follow broadly the same lines as in the United Kingdom with three important exceptions:

1. Taxes on capital gains are included under the heading of casual sources.
2. There are no provisions corresponding to the system of deduction at source in the United Kingdom, whereby the liability to tax on rents, interest, annual payments or dividends is satisfied by a deduction of tax made by the payer.
3. In the case of trades or businesses, the profits are charged on a current-year basis. When the accounts are made up to a date other than 31st December, the profits charged are the profits of the accounting year ending immediately before 1st March in the "assessment year." This is the year in which the assessment is made, and it is thus the year following the year for which the tax is charged.

The basis of taxation of capital gains varies according to the duration of ownership. In the case of real estate, where the taxpayer has owned the property for less than seven years 100 per cent of the profit is taxed. For every year of further ownership the profit charged is reduced by 25 per cent, and where the property has been held for more than ten years there is no liability to tax.

In the case of other securities and capital assets held for less than two years, 100 per cent of the profit is taxed, and again the profit charged is reduced by 25 per cent for every further year of ownership until they have been held for more than five years, when there is no liability.

Swedish officials and authors occasionally refer to "tax at source" or "deduction of tax at source" as a feature of the Swedish system, but they mean by that phrase the system of collection of preliminary tax (*preliminär skatt*), which is a payment on account of a liability to be determined later. This system has been fully described in Chapter 3. There is in Sweden no universal system of deduction of a standard rate of tax at source from rents, dividends, interests and annuities, such as obtains in the United Kingdom.

There is no deduction of tax from dividends paid to Swedish residents. Although dividends are paid out of profits which have already suffered communal and state taxes, they are charged again as income in the shareholders' hands without any deduction for taxes paid by the company. There are no deductions of tax from mortgage or other interest or from annual payments. Instead deductions are made in computing the payer's income, as is done in the United



## THE MAIN FEATURES OF THE SWEDEN INCOME TAXES

Kingdom in the case of interest payable to banks and building societies.

Deductions allowed from income consist of annuity, pension and life assurance premiums, payments to dependants not resident with the taxpayer, and those losses which are deductible in the same year from income from other sources. The maxima for life insurance premiums are kr. 200 for a single person and kr. 400 for a married couple. There is an exemption for the first kr. 300 of a wife's earned income. The balance after such deductions constitutes the taxpayer's assessed income.

A deduction is given for a "family allowance," which is intended to even out differences in the cost of living and is highest where costs are highest. There are four groups of localities. The allowance given varies from kr. 1,230 to kr. 1,400 for single persons and from kr. 1,760 to kr. 2,000 for married persons, according to the area of residence.

Converted into sterling at kr. 14.5 to the £, these allowances represent very small amounts of income. It follows that virtually every employed person, and every person having a pension or investment income sufficient for maintenance, is liable to communal income tax.

Where the wife has income she makes a separate return and the family allowance is apportioned between husband and wife. Women income taxpayers in Sweden number rather more than one-third of the total: 1,310,119 in 1952 out of a total of 3,735,086. Family allowances for communal income tax are given only against income assessed in the commune of residence. A resident in Stockholm whose only income was derived from a business in Malmö would receive no family allowance.

The rates of tax vary according to the budgetary needs of the local authorities. The tax is not progressive, there being one flat rate for all income whether earned or unearned. Companies pay at the same rate as individuals. In Stockholm the present rate is about  $10\frac{1}{2}$  per cent of taxable income. This is a little lower than the general average for the whole country which is about 12 per cent.

### STATE TAXES ON INCOME

The State Income Tax Law imposes state income tax by reference to the definitions of income which are found in the Communal Tax Law, the only substantial differences being that communal income tax is treated as a deduction in computing income taxable to state income tax, and that the family allowances for state tax are on a more substantial scale. The state income tax on companies is now at the rate of 50 per cent. On individuals it is highly progressive: the scale for single persons rises from 13.2 per cent on the first kr. 4,000 of taxable income to 65 per cent for all income over kr. 150,000; for

married persons, 13.2 per cent is paid on the first kr. 8,000 of taxable income, rising again to 65 per cent for all income over kr. 150,000.

While there is no differentiation in income tax between earned and unearned income, all capital owned in excess of kr. 50,000 (at current rates of exchange £3,448) is liable to an annual tax. The definition of capital is widely drawn and includes all forms of real estate, stocks, debentures and bonds, bank deposits and other loan holdings, jewellery, motor-cars, and yachts. It does not include furniture and domestic equipment in the home, nor private collections of works of art and books. There is a gradual progression from 0.5 per cent on capital exceeding kr. 50,000 but less than kr. 100,000, to 1.8 per cent on all capital exceeding kr. 1,000,000. There is a special relief where the total assessed income is less than  $3\frac{1}{3}$  per cent of capital assets, in which event tax is levied on 30 times the total income or one half of the capital value, whichever is the higher. Debts and borrowed money are deducted in computing capital.

There are also some specialised state taxes in the nature of taxes on income which fill certain gaps in the fundamental tax laws. These taxes do not seem to have any bearing on the main subject of this report. They are:

- (a) The coupon tax on certain dividends, mainly Swedish company dividends paid to non-residents;
- (b) The sailors tax on the earnings of seamen employed on certain Swedish merchant ships who are not liable to the normal income tax;
- (c) The tax on lottery prizes;
- (d) The tax on foreign theatrical artistes and public entertainers;
- (e) The tax on distributions in connection with the reduction of share capital or the winding-up of a company;
- (f) The tax on the undistributed income of companies.

Finally, the total taxes (property tax, income tax and capital tax) payable by a taxpayer for any period must not exceed 80 per cent of his taxable income for that period.

An analysis of assessments and tax levied under the state income tax law for 1953 is given in Appendix I, Table 6. An equally detailed analysis of communal income tax assessments is not available, but owing to the close affinity between the bases of the two taxes, conclusions can safely be drawn from Table 6 as to the relative yield from different types of taxpayer.

The proportion of assessments to communal income tax attributable

## THE MAIN FEATURES OF THE SWEDISH INCOME TAXES

to different classes of taxpayer is found in Table 4 of the *Skattetaxeringarna* for 1954 issued by the *Statistiska Centralbyrån*, Stockholm.

The attribution in million kroner is as follows:

<i>Assessed income</i>	
Individuals	25,260.2
Joint stock companies	2,028.1
Swedish economic associations	57.6
Other associations	228.6
	<hr/>
All taxpayers	27,574.4
	<hr/>
<i>Taxable income</i>	
Individuals	19,979.8
Other taxpayers	2,314.3
	<hr/>
All taxpayers	22,294.1
	<hr/>

## THE TREATMENT OF FOREIGN INCOME OF SWEDISH RESIDENTS AND THE SWEDISH INCOME OF FOREIGN RESIDENTS

The rules relating to the treatment of foreign income of Swedish residents and the Swedish income of foreign residents are, broadly speaking, the same for communal and national tax purposes, and the description given below relates to both taxes. Any important differences of treatment are noted.

Where the foreign income of Swedish residents and companies is derived from invested capital or from businesses independently carried on abroad, it is chargeable to the communal tax as income from capital. Where the income is derived from business activities which are part of an organisation managed and controlled in Sweden, the profits are assessed as profits from business.

Foreign members of foreign embassy or consular staffs in Sweden are treated as not domiciled in Sweden. A Swedish national on the staff of a foreign embassy or consulate in Sweden is exempt from tax on the emoluments of his employment.

Residence for tax purposes is not determined by the registration for census purposes (*mantalsskrivning*) but by the place of residence during the income year, i.e., the year in which the income was enjoyed, not the fiscal year. Residence involves having an actual home in Sweden. A Swedish citizen who travels extensively abroad but whose home or family remain in Sweden is taxed as a resident. Swedish nationals who have taken employment abroad may still be registered in Sweden for census purposes, but if they have settled down more



or less permanently abroad and have not retained a home in Sweden, they are not resident for tax purposes.

The Swedish income of foreign residents which is chargeable with tax under the Swedish law is assessed wholly in Stockholm, and the communal tax is credited to the account kept for combined communal purposes which is to be applied to the equalisation of tax between the various communes. The present rate of communal tax on such income is 5 per cent, with no family allowance.

Foreign corporations which are deemed to be Swedish residents by reason of the central control and management being in Sweden are allocated for communal tax purposes to the commune where control was exercised on 1st November in the year preceding the year for which the tax is charged. Foreign states, communities, insurance companies and other companies not incorporated in Sweden are treated as foreign corporations.

Swedish nationals employed abroad in the consular and diplomatic service are treated as persons domiciled in Sweden but are not taxable on their consular or diplomatic salaries.

The tax is levied, in principle, on all income of which the source is regarded as localised in Sweden.

A non-resident is required to make a return without prior demand if his gross earnings from Sweden amounted to kr. 100, or he possesses assets liable to property tax of a value exceeding kr. 50,000.

Income from services given in Sweden by a non-resident is liable to Swedish tax only if payment is also made in Sweden, but even this restricted power to require a return does not extend to fees for casual work, such as broadcasting, or occasional work for newspapers.

An individual not resident in Sweden has also to suffer Swedish coupon tax on dividends on shares in Swedish companies. There are special rules for seamen.

All foreign bodies of persons, whether corporate or unincorporate, are treated in Swedish tax law as foreign companies. In the case of companies, liability does not depend upon residence. A company is a Swedish company for taxation purposes if it is registered as such under Swedish law. If, as in the case of certain societies, the law does not require registration, the determining factor is whether the controlling board has its seat in Sweden or if the main activities are carried on in Sweden. Foreign companies are such companies and bodies of persons as are not registered in Sweden and are controlled by a board or council meeting outside Sweden.

Swedish companies are liable to tax on the whole of their incomes. Foreign companies and bodies of persons which are deemed to be

#### THE MAIN FEATURES OF THE SWEDISH INCOME TAXES

foreign companies are, like non-resident individuals, liable only on their incomes arising in Sweden.

There is a general power residing in the King in Council to remit national income tax on compassionate grounds, or for other special reasons, where foreign income has been subjected to double taxation and where there is no governing Double Taxation Convention. But the main method of dealing with the problem is through the large number of conventions on a reciprocal basis which have been concluded with other countries. These agreements are concerned primarily with the national tax, and the extent to which they affect the communal tax is far from clear. This matter is discussed in greater detail in Chapter 9.

## Chapter 5

### OTHER LOCAL REVENUES FROM TAX SOURCES

#### EXCHEQUER GRANTS

IN Sweden 23 per cent of the total tax-borne expenses of local government in 1951 was met by exchequer grants (*Statsbidrag*). Details of these grants are contained in Appendix I, Table 4. The remaining 77 per cent was defrayed out of the yield of the local taxes. In the United Kingdom exchequer contributions in that year accounted for one-half of the total tax-borne expenditure, so that there is considerably greater dependence of local authorities on national funds in the United Kingdom, a circumstance which carries with it the exercise of greater control by the government departments over local administration. Local authorities in Sweden are not so dependent upon exchequer grants and to that extent are less likely to be subject to central control.

Exchequer grants yielded kr. 599 millions in 1951. The education grant is overwhelmingly the largest. No less than kr. 431 millions, or 72 per cent of the total grants, was on education account. The greater part consists of the reimbursement of teachers' salaries. Part of the education grant consists of a percentage of expenditure, for example on the provision and maintenance of buildings. The percentage varies according to the taxable income per inhabitant, the higher the income the smaller being the grant percentage. The table of income per head was fixed in 1945 and has not been amended since, and local authorities complain very insistently that, as a result of the pressure of inflation and rising money incomes since that date, they have been moving steadily down the percentage scale of the grant.

Next in order of magnitude is the health services grant, applicable mainly to the hospitals provided by the councils of the counties and the six largest cities. The grant amounted to kr. 53 millions. There are grants also for police, roads, welfare, rural water supplies, and other services. Only in education does the exchequer grant account for more than a small part of the local authorities' expenditure. There is a movement among local authorities in Sweden to seek the abolition of the separate service grants and to institute in their place a single block grant which would be calculated on some formula designed to



## OTHER LOCAL REVENUES FROM TAX SOURCES

meet fairly and suitably a proportion of the costs to be borne by local government.

### TAX MITIGATION GRANT

Reference has already been made in Chapter 2 to the Tax Mitigation Grant (*skattelindringsbidrag*). While it may be compared with the Exchequer Equalisation Grant in the United Kingdom, the comparison should not be carried too far because the Swedish grant is diminished by a factor which takes into account the average expenditure per head, while in the United Kingdom the equalisation grant is designed to raise the income resources of the under-average authorities, and the measure of the shortfall of income resources is then applied to the whole expenditure of the authority in order to compute the amount of the grant. The Tax Mitigation Grant does not feature so prominently as does the equalisation grant in local government in this country. In 1951 it amounted to kr. 4,143,000, equal to only £286,000, quite a negligible sum and equivalent to something of the order of £2,000,000 on the population of the United Kingdom. Its smallness compared with the equalisation grant is due to the terms of the grant formula and to the smaller dispersion of rates of tax in Sweden.

The moneys for the grant come from the assessment to communal income tax of income and profits arising from activities in Sweden of non-resident persons. These persons with no permanent establishment in Sweden are taxed in Stockholm for combined communal purposes at the rate of 5 per cent. The receipts are paid into the Tax Mitigation Fund (*skattelindringsfonden*) administered by the Government, which may also contribute moneys out of national taxation.

The working of the grant is complicated. The first step is to ascertain the taxable income per inhabitant of the local authority, which is then compared with the average for Sweden as a whole. Those authorities which are under the national average are eligible for grant. The main factor in the calculation of grant is the amount, expressed as a proportion, by which the income per inhabitant of the local authority falls short of the figure for the whole country. It is similar to the "rateable value credited" in the Exchequer Equalisation Grant. Thus, if the income per inhabitant of the local authority is kr. 1,200 and the national figure is kr. 1,600, the shortfall proportion is 25 per cent. The government then becomes responsible for that proportion of the expenditure of the local authority; not wholly, but only for that part of the expenditure which is in excess of what would be the yield in the local authority area of the national average rate of communal income tax calculated on the actual income per inhabitant

of the local authority. In other words, the communal taxpayers in the local authority area must first of all meet in full an expenditure equal to the product of the national average rate of communal tax, and the balance of expenditure is divided between them and the government, with the government meeting the shortfall proportion. The government contributes the shortfall proportion only of the tax required beyond the national average rate of tax. The national average was taken at kr. 11 per skattekrone in 1950, when it was raised from kr. 10 per skattekrone. This figure still remains, although taxes have increased since then.

An example of the operation of the grant is given in Appendix II. The local authority in the example has tax-borne expenditure of kr. 216 per head and a taxable income per head of kr. 1,200. Without state aid the rate of tax would be kr. 18 per skattekrone. The national income per head is kr. 1,600, so that the shortfall is kr. 400 or 25 per cent. Taking in the first instance the expenditure covered by the national average tax rate of kr. 11 per skattekrone, an amount of kr. 132 is arrived at, leaving kr. 84 to be divided, 75 per cent or kr. 63 to the inhabitants and 25 per cent or kr. 21 to the Government. The share of the tax expenditure borne by the inhabitants is therefore kr. 195 per head which, on an income per head of kr. 1,200, requires a tax rate of kr. 16.25 per skattekrone, and the government pays kr. 21, which is equivalent to a tax rate of kr. 1.75 per skattekrone. The Tax Mitigation Grant is thus kr. 168,000.

According to the Financial Secretary of the Union of Rural Authorities, the grant is in fact calculated not upon the national average taxable income per head, but upon that average less 20 per cent. Almost the whole of the Tax Mitigation Grants are paid to rural communes in Norbotten, the most northerly province in Sweden, lying beyond the Arctic Circle. The figure was kr. 3,701,000, out of a total grant of kr. 4,143,000. The balance was almost entirely to communes in Västernorrland and Västerbotten, also provinces of the far north.

#### MINOR LOCAL TAXES

There are one or two minor taxes levied by local authorities—entertainment tax, dog tax and artistes tax. The entertainment tax is the most important of them. Altogether in 1951 they produced kr. 28 millions (about £2,000,000). These minor taxes contributed only 1.5 per cent of the total revenue from local taxes, and their yield is very small compared with that of the communal income tax which in 1951 produced kr. 1,952 millions.

#### OTHER LOCAL REVENUES FROM TAX SOURCES

The entertainment tax is administered locally by the primary authorities and is charged at scales fixed by the government. It is really a series of taxes, different rates applying to different kinds of entertainment and different rates apply to different prices. In cinemas the tax is 30 per cent of the gross price up to kr. 1, and 45 per cent beyond kr. 1. The tax in theatres is 15 per cent.

Local authorities do not retain the whole yield of the entertainment tax, but hand over to the government, through the provincial governor's office (*länsstyrelse*), a proportion of the revenue. In the case of cinemas, three-quarters of the total is paid over to the state and one quarter is retained. In other cases the tax yield is divided equally.

There are provisions for remitting the tax on entertainments for charitable and other approved purposes. The commune may remit only its share and the provincial governor may remit his share. There is always prior consultation in order that each may come to the same decision.

The government lays down minimum and maximum rates for the dog tax, within which the communes have discretion to fix the rate to be charged locally. The present maximum rate is kr. 50. The whole tax is retained by the local authority.

The artistes tax is charged on artistes who are not resident in Sweden and do not pay Swedish income tax. Artistes who are resident in Sweden pay taxes, communal and national, in the ordinary way. The tax on artistes yielded in 1951 only kr. 295,000 or £20,000. It is calculated at a percentage on the fees received or the receipts of the concert, depending on whether the artiste organised the concert or only took part in it.



## Chapter 6

### LOCAL AUTHORITIES AND THE COMMUNAL INCOME TAX

THE communal income tax is of overwhelming importance to local authorities in Sweden. In the present chapter the working of the communal income tax is considered from their point of view.

It has been explained how each local authority fixes its own rate of communal income tax, and how thereafter it is dealt with by the national tax organisation. Outside the six cities, which are themselves county councils, the communal income tax consists of two parts, one part determined by the primary commune and the other by the county council. Thus in Alingsås in 1952, the total local tax of 14.99 per cent was made up of 11.99 per cent for the primary commune and 3.00 per cent fixed by the county council of Älvsborgs Län. In Sweden there is no system whereby the county council precepts on the primary communes in its area: the county council raises its own revenue through the national (and local) tax machine in the way described.

#### RATES OF COMMUNAL INCOME TAX

Income tax is always expressed as a rate per skattekrona, one skattekrona being kr. 100 of taxable income. A tax rate of 10.94 is kr. 10.94 for every kr. 100 of taxable income. It is thus simply a percentage of the income on which the tax is computed.

The communal income tax rates for 1950 were as follows:

	<i>Average</i>	<i>Highest</i>	<i>Lowest</i>
Cities (including county)	12.70	16.75	10.00
Market towns (excluding county)	8.91	—	—
Rural communes (excluding county)	8.59	10.99	7.03
Counties	4.04	5.60	3.00

The average rate for the whole of Sweden for 1952 was about 12.75. The *Statistical Year Book* gives separate figures for each of the cities and counties, but does not do so for the market towns and rural communes. The rates given in the foregoing table for the highest and lowest in the rural communes are provincial averages for all the rural

## LOCAL AUTHORITIES AND THE COMMUNAL INCOME TAX

communes in each province. Thus the "lowest rate" of 7.03 is in fact the average for all the rural communes in Kronobergs Län, and the "highest rate" of 10.99 is the average for the rural communes in Norrbottens Län. The rates for Stockholm and Göteborg were 10.94 and 12.00 respectively.

From these figures one would like to come to a conclusion as to the dispersion in the rates of communal income tax in order to make a comparison with the dispersion of local rates in the United Kingdom. Dispersion in Sweden could arise, among other causes, from the methods adopted to allocate to each commune profits arising in two or more communes, from variations in the profit-making capacities of the different industries spread throughout the land, and from the situation of these industries. Without the separate rates for all local authorities the dispersion cannot be computed properly, but an attempt to arrive at a feasible basis of comparison is made on the figures set out above.

In the case of the cities, the rates of communal tax (including the county tax) range from 10.00 to 16.75. The total range is thus 6.75, which represents 53 per cent of the average rate of 12.70. These figures relate to 1952. In the return of local rates for England and Wales for 1954-55, published by the Institute of Municipal Treasurers and Accountants, the following figures are given:

	<i>Average</i>	<i>Highest</i>	<i>Lowest</i>
County boroughs	23/2	28/-	15/-
Metropolitan boroughs	20/7	23/8	17/4
Non-county boroughs	23/9	28/6	19/-

In the case of the county boroughs, the range from 15/- to 28/- (i.e., 13/-) represents 56 per cent of the average rate of 23/2. For metropolitan boroughs and non-county boroughs, the corresponding figures are 31 per cent and 40 per cent. There appears therefore to be about the same dispersion in rates of communal income tax in Sweden as in poundage of local rates in the United Kingdom.

It might have been expected that a tax based on the annual value of land and buildings would show a smaller variation in tax rates from one area to another than a tax based on profits, wages and other income. The similarity in the dispersion of tax rates is the more remarkable when one has regard to the magnitude of the Exchequer Equalisation Grant in the United Kingdom, which has the effect of reducing poundage variation. In 1951-52, the Exchequer Equalisation Grant amounted to £54,000,000. The total receipts from local rates

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amounted to £332,000,000. The Tax Mitigation Grant in Sweden in 1951 amounted only to kr. 4,143,000, compared with communal income tax of kr. 1,952,231,000. This paragraph is, of course, concerned with variations in the rates at which the taxes are levied, not with the amounts that are paid by the different groups of local tax-payers.

The rates of communal income tax in the cities were remarkably steady between 1944 and 1950, being 8.47, 8.45, 8.34, 8.43, 8.75, 8.54 and 8.79 for consecutive years. The rate jumped up to 10.53 in 1951 and to 10.75 in 1952 (these are preliminary figures). This degree of continuity is shown also in the market towns, rural communes and counties where, too, the rise in 1951 and 1952 is noticed. The increase in the cities from 8.47 in 1944 to 10.75 in 1952 is equal to 27 per cent. The 1951-52 return for England and Wales, referred to previously gives the following figures:

	<i>Rateable value</i>	<i>Rate income</i>	<i>Per £ rateable value</i>
1943-44	£317,000,000	£204,000,000	12/10
1951-52	335,000,000	318,000,000	19/-

The rise in the average local rate poundage levied between 1944 and 1952 was 6/2d. or 48 per cent, notwithstanding in 1948 the severance of hospitals and public assistance from local government. The greater rise in local taxes in the United Kingdom is due partly to the comparative inelasticity of the property basis. In Sweden inflation has had a direct effect upon the income basis of local taxation, and the comparative steadiness of the rates of communal income tax in the years under review is due to income having increased more closely with expenditure than has the annual value of property in the United Kingdom. Provided that the level of economic activity continues with nothing more serious than minor fluctuations, an income basis for local taxation is likely to result in a greater degree of continuity in the rates at which, year by year, the local taxes are imposed. During the last few years there has been a great outcry in the United Kingdom about the rise in local rates and the insupportable burden they have become on the ratepayers. It is doubtful if, in fact, local government expenditure is any greater a proportion of the national income than it was in the pre-war years. Part of the problem may be psychological, because people cannot bring themselves easily to accept a local rate of 25/- as normal, even though it is no larger a part of their income than the local rate was before the war. Local rate poundages have a special significance, and local councillors are well



## LOCAL AUTHORITIES AND THE COMMUNAL INCOME TAX

aware of the watchful attitude of the ratepayers who live on their own doorsteps. A local tax structure, such as the Swedish communal income tax, which responds directly to rises in the national income, would remove part at least of this aspect of the local councillors' troubles.

### STABILITY IN TAX BASE

In local government there are two elements which, among others, are required for sound financial administration. They are stability in the financial resources and certainty in the yield of the taxes. The use of property as the basis of local tax in the United Kingdom does impart stability and certainty to the local government financial structure and to the individual local authorities. This is a most valuable attribute of the present local rating system and if, in addition, the distribution among ratepayers of the burden of local rates can be regarded as equitable, then it is a system which has notable advantages. It has been noted that the Swedish system of communal income tax has worked very well and that it has displayed a large degree of stability. The post-war years, however, have been years of steady and growing economic prosperity, and it is no wonder that such a fine record of financial steadiness has been the outcome. Unfortunately there may also be lean years and it is necessary to consider how a local income tax system would fare in such circumstances.

The Swedish Government has directed local authorities to contribute sums into tax regulation funds, no doubt prompted partly by this possibility. No such funds, however, could carry local authorities through a long period of economic slump. Profits and incomes would fall, and so too would the taxable resources of the local authority. The communal tax rates would require to be raised. The views of persons engaged in local government were sought on this matter. They felt that the system could withstand fairly easily minor recessions in economic activity. They pointed out that, even if a major recession took place, the taxes still would be levied according to ability to pay, so far as that is measured by income, and that the difficulties would be no greater than would confront local authorities in the United Kingdom. Indeed, because of the integration of the communal and national income taxes, the communal income tax being a deduction from income for national income tax purposes, the financial difficulties of local authorities would be passed on to the government. Their opinions were that it was not necessary to frame a system of taxation designed particularly to overcome the difficulties of trade depression, that their local system, integrated with the national system, worked

satisfactorily and was probably more able than most others to cope with the problems of a slump in trade.

There are one or two communes in Sweden which are dependent upon one industrial enterprise. Sandviken has already been mentioned. There is another, Sura, which is wholly dependent upon the *Sura Hamnar Järnverk* (ironworks). If the ironworks were out of work the whole community would suffer and the greater part of the income of the commune would disappear. This would happen, of course, even if the commune's income were based on the value of property. In fact the ironworks are owned by the great Swedish ASEA company, which could take steps to assist the commune in more ways than one. The company has an interest in promoting the welfare and financial stability of the commune and, according to Professor Heckscher, might declare such a part of its total profits in Sura as to achieve this object. For many years the company undertook at its own cost the administrative work of the council of the commune. Later on, as a separate civic consciousness developed, the council took over the administrative work itself at a cost several times greater than before.

#### NUMBER OF COMMUNAL INCOME TAX PAYERS

A matter of importance is the number of persons who are required to contribute towards the cost of the community services provided by the local authority. In both the United Kingdom and Sweden they do so in two capacities: as national taxpayers through the medium of Exchequer grants, and as local taxpayers and ratepayers. They contribute as national taxpayers to a greater extent in the United Kingdom than in Sweden. It is probably right that this should be so, the regressive nature of the rating system being mitigated by the large sums contributed to local government out of national funds which are derived to the extent of fully one-half from income taxes and estate duties.

Many persons in the United Kingdom, by the operation of the personal allowances, do not pay any income tax, but if they are householders they do not escape payment of local rates. In all communities, all households and businesses contribute to the local rate fund, and in return the whole community shares the municipal services. If householders demand more services, then they must reckon the cost, because they are called upon as ratepayers to meet part, at least, of the cost. In this way there is a concurrence of benefit and liability which, though not wholly equated, promotes the careful management of civic affairs. If, in a system of communal income

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tax, many members of the community were exempted by deductions made in arriving at taxable income, then the danger might arise that too many beneficiaries would make demands upon too few contributors. There should be a reasonably close identity between enfranchisement and financial responsibility.

In Sweden the personal allowances for communal income tax are low and few persons in gainful employment escape liability.

A matter of vital concern to local authorities is the allocation among communes of profits of businesses conducted from establishments in several local authority areas. The bases of allocation, which are contained in the communal income tax statute (*kommunalskattelag*), are dealt with in Chapter 8.

The communal and the national income tax are administered together, and local authorities' administrative duties end with the fixing of the rate of the local tax. The amount of communal income tax paid is deducted from income for assessment to national income tax. This has the effect of transferring a further part of the cost of local government to the national exchequer. If no such deduction were granted, the rate of national income tax would be lower.

One comes to the conclusion that in Sweden, as compared with the United Kingdom, local government is less subject to central control because the exchequer grants are a much smaller part of income, that the Swedish local taxes are not regressive in the way the British local rates are, that the Swedish communal tax system is designed to bring in as local taxpayers virtually all who receive incomes, and that it is working with as much acceptance as any tax system is ever likely to be accorded.

### LOCAL TAXATION PER HEAD

In 1951 the total income of local authorities in Sweden from tax sources was kr. 2,579 millions, made up of exchequer grants of kr. 598 millions and local taxes of kr. 1,981 millions. For that year the population was 7,099,000, giving an expenditure per head of kr. 363 or £25. In England and Wales in 1951-52 receipts from exchequer grants amounted to £350 millions and local rates yielded £332 millions, giving a combined total of £682 millions representing £16 per head. Taking the local taxes and rates by themselves, the expenditure per head met out of local taxation is kr. 279 or £19 in Sweden and £8 in the United Kingdom. The difference is of interest, especially in view of the complaints that the British rating system, which accounts for only one-half of the tax-borne expenditure, has reached a critical stage and, because of its regressiveness, is weighing too heavily on large sections of ratepayers.



## INTRODUCTION OF LOCAL INCOME TAX IN UNITED KINGDOM

From the local authorities' point of view, one of the most important issues to which a local income tax gives rise is the division of profits among several communes. The fewer and larger the communes, the less difficult becomes the allocation of profits. Carried far, the enlargement of local authorities would mean the end of local government, a development which would certainly arouse the greatest opposition. The contiguity and overlaying of separate local authorities in London and other conurbations in the United Kingdom, giving rise to difficulty in the allocation of profits and holding the probability of inter-communal differences, is an obstacle in the way of the introduction of a local income tax. This problem is very much less acute in Sweden. The present boundaries of British local government areas would require to be considered in the light of the location of the industrial areas. The distribution of functions among the different kinds of local authorities might also require to be taken into account. In England and Wales, county councils precept upon district councils, while in Scotland county councils, which are rating authorities themselves in the landward areas, requisition upon the burgh councils. In Sweden the county council administers the same services throughout the whole county and fixes its own rate of local tax, with no precepts or requisitions. The introduction of local income tax in the United Kingdom might well require the adaptation of the local government system.

## Chapter 7

### RELATIONSHIP BETWEEN THE COMMUNAL AND STATE INCOME TAXES AND THE EFFECTS OF THE COMMUNAL INCOME TAX ON THE LOCATION OF INDUSTRY, ETC.

This chapter deals with a number of particular points of interest affecting the Swedish communal income tax.

We have already drawn attention to the fact that the communal income tax is allowed as a deduction in computing income for state tax purposes. We were surprised to find no cognizance of the fact that this means that communities having a preponderance of residents in the upper income ranges are in fact receiving a hidden grant from the state towards the cost of their local services. As the deduction is effective on the top slice of each taxpayer's income, it follows that the state suffers a greater relative loss of tax in the case of high incomes, amounting to as much as 65 per cent, than in the case of low incomes, which may be exempt or liable to state tax at the lowest rate of only 13.2 per cent. In effect the state bears a progressive share of the cost of local services as the income of the individual increases.

In all probability Swedish taxation theory, in which the rights of the provinces are paramount, is based upon the principle that national tax should be related to the income left after providing for the cost of local services. It seems doubtful whether this is a sound concept, as it has a tendency to induce rich people to move from areas occupied by people of varied incomes into areas more exclusively the preserve of the well-to-do.

If the rate of communal tax is increased to meet a higher level of expenditure, a larger deduction is made from national taxable income and the government may be obliged to increase the rate of national income tax. In this way the two rates of tax, communal and national, react upon each other. To a limited extent the same interaction exists in the United Kingdom in the deduction of rates in computing trade profits for the computation of income tax, but the full effect is only felt in the case of shops and offices. In Sweden, where the deduction of communal tax extends to employees and private residents, there is a much closer correlation of the two taxes.

## THE FINANCE OF LOCAL GOVERNMENT IN SWEDEN

An example of the inter-relation of the communal and national income tax systems is given in the booklet issued in 1954 by the Taxpayers' Society (*Skattebetalarnas Förening*), taking a married couple living in cost of living area 5, with a net assessed income of kr. 20,000.

<i>Communal Income Tax</i>		
Assessed net income	kr. 20,000	
Personal allowance	2,000	
	<hr/>	
Taxable income	18,000	
Communal income tax at 12.00		kr. 2,160
<i>National Income Tax</i>		
Assessed net income		kr. 20,000
Personal allowance	kr. 4,000	
Communal income tax paid	2,160	6,160
	<hr/>	<hr/>
Taxable income		13,840
National income tax—		
kr. 1,848 + 27.5 per cent of kr. 1,840		kr. 2,354
		<hr/>

If no deduction were given for communal income tax paid, the taxable income would be kr. 16,000 for national income tax purposes, and the taxpayer would still be within the 27.5 per cent rate on the top of his income. As a result of the set-off of the communal income tax paid, his national income tax is reduced by 27.5 per cent of kr. 2,160 or kr. 594.

Local income taxes paid by companies reduce profits, which are taxable at 40 per cent (now 50 per cent). The local taxes paid by the lowest income groups of individuals have no effect on the state revenues, as those groups, owing to the higher family allowances for state taxes, are not liable, or only insignificantly liable, to state tax. On the other hand the local taxes paid by the truly wealthy are compensated to the extent of as much as 65 per cent by a reduction in state tax. The state is therefore much more closely concerned with any over-provision of local services in wealthy areas than in those populated by the poorer classes.

Variations in rates of tax from one commune to another may have some influence on the location of industry, but it was impressed upon us that this was by no means the most important factor. More concrete inducements in the shape of preferential rates for carriage or power, or agreements to provide housing and amenities for workmen, could easily outweigh the tax factor.



## RELATIONSHIP BETWEEN THE COMMUNAL AND STATE TAXES

The knowledge that a multiplication of selling points leads to greater complications in tax computations may well tend to encourage forms of trade in which the actual sale of goods is concentrated in a few spots, though delivery may be from points more numerous than those at which sales are effected, but this is a minor factor. The physical facts, transport, labour, storage facilities, count for much more in this connection than tax factors.

As the rate of communal income tax varies from 16.75 per cent in Kramfors to 10.0 per cent in Skanör-Falsterbo, where the taxpayer's private circumstances permit him any choice, there is some inducement to take up residence in the areas of low taxation. The inducement is less than might at first sight be expected, because the allowance of the communal tax as a deduction in computing the national tax diminishes any advantage the wealthy taxpayer (who is of course the person most likely to be affected) would enjoy by moving his residence. Nevertheless, we did find some critical comment on this matter.

## Chapter 8

### THE MAJOR DIFFERENCES BETWEEN SWEDEN AND THE UNITED KINGDOM IN THEIR METHODS OF ADMINISTRATION AND THE BASIS OF ASSESSMENT OF INCOME TAX

THIS chapter is confined to a discussion of such differences as have a bearing on the introduction of a local income tax into the United Kingdom. In our next chapter we consider what effect these differences would have on a local income tax in the United Kingdom.

In Sweden local autonomy in taxation, resting on the power to fix the rate of communal income tax, is also reflected in the form of the administration of the tax. The Swedish assessment boards, unlike their counterpart in this country, the Additional Commissioners of Income Tax, actually undertake the task of reviewing all the returns and making the assessments. While the chairmen are nominees of the provincial governors, they are unpaid private citizens and the character of the work they do is affected by their status. In the United Kingdom the influence of the central Inland Revenue authority is much more closely felt. The Inspector of Taxes and his staff do the actual work of assessment, subject to differing degrees of control by the lay bodies of additional Commissioners. Central control is firm and authoritative, and no substantial departure occurs from the practice approved at the centre. The British scheme of taxation is more complex and elaborate than that of Sweden, and this has had the inevitable effect of lessening the extent to which lay bodies can take an effective part in the administration.

Local autonomy also makes its influence felt in another direction. We were told that each *taxeringsintendent*, the official nearest in function to the Inspector of Taxes in the United Kingdom, makes decisions and gives rulings independently of his colleagues in other areas, subject to appeal to the *provvningsnämnden* and, in important cases, to the Court of Exchequer and the Supreme Court. It was not made clear to what extent differences in practice exist in different parts of Sweden or whether the differences are serious, but such variations between one area and another do not occur in the United Kingdom.

## DIFFERENCES BETWEEN SWEDEN AND U.K.

These variations stem from the Swedish principle of *självstyrelse*—the independence of the local community from undue central control.

Further differences between the Swedish and the British systems can conveniently be set out in parallel columns. (The tax rates quoted for the United Kingdom relate to 1954–55.)

### SWEDEN

### UNITED KINGDOM

#### *Exemption Limit and Family Allowances*

The exemption limit for communal income tax in Sweden is very low, the equivalent in sterling for a single person being less than £100, and for a married couple less than £140 with an additional £20 for a wife's earned income. This results in all full-time and most part-time workers being liable and leads to a wide spread of direct taxation. The total population of Sweden in 1950 was 7,046,920 and the number of income tax payers in 1952 was 3,735,086. Thus 50 per cent of the population of Sweden are required to make an annual income tax return.

The local variations in the amount of the family allowances do not seem to have any bearing on the possible introduction of a local income tax in the United Kingdom. Larger allowances in areas where the cost of living is higher are theoretically sound, but this is not an essential feature.

The statistics show that for 1951–52 there were 20½ million individual incomes within the range of taxability, i.e., from £135 per annum upwards, but approximately 20 per cent of these incomes have no tax to pay. Returns are not called for annually over the whole of the PAYE field. A total of approximately 15½ million persons made returns out of a total population of 50½ millions.

Owing to subsequent changes in the PAYE system, it is expected that in future only about 12½ million individuals in any year will make returns of total income.

There is no local variation in the amount of personal allowances in the United Kingdom.

#### *Differential Rates of Tax*

Each commune has a uniform rate of communal income tax. The tax is therefore proportional and differs in its incidence from United Kingdom income tax.

In the United Kingdom graduation of tax on small incomes is effected by differential rates. The income, after deducting the personal allowances, is taxed as to the first £100 of taxable income at 2/6d. in the £, the next £150 at 5/- in the £, the next £150 at 7/-, and only the excess over these amounts at the full standard rate.



## THE FINANCE OF LOCAL GOVERNMENT IN SWEDEN

### SWEDEN

The distinction between earned and investment incomes is achieved by the annual tax on the invested capital of individuals. This does not operate at low levels, as only capital in excess of kr. 50,000 (£3,448 sterling) is taxed. The tax is also progressive, the rate charged increasing for each successive slice of capital up to kr. 1 million.

The Swedish national income tax is also highly progressive, rising from 13.2 to 65 per cent for the highest slices of income.

### *Husband and Wife*

In assessing communal income tax, the higher scales of family allowances from kr. 760 to 2,000 are divided proportionately between the income of husband and wife. As these allowances are only 43 per cent higher than the allowances for a single person, the basis bears rather heavily on married couples. The additional allowance of kr. 300 given to a wife against her earned income serves to reduce the disparity but does not equalise the position. In the area of highest allowance, the single person's allowance is kr. 1,400, while the married couple's allowance plus the wife's earned income allowance amount only to kr. 2,300.

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The difference in taxable capacity between earned and investment income is recognised by reducing by 2/9ths the amount of earned income upon which tax is charged. An earned income of £1,800 per annum bears the same amount of tax as an investment income of £1,400.

In the United Kingdom, £120 is allowed to a single person, and £210 to a married couple with an additional allowance to a wife against earned income not exceeding £120. There are also extensions of the reduced rate where the wife has earnings in excess of £120. The overall effect is a considerable inducement to married women in the lower income ranges to take employment, in contrast to the system in Sweden where the tax inducement is small and the tax payable by a husband and wife both having earned income is likely to be much greater than if they were separately assessed as single persons.

These comparisons are confined to persons below the surtax limit of £2,000, as above that limit the aggregation of income introduces a new factor.

### *Deduction of Tax at Source*

This question is of great importance as it influences the place where the tax is paid. In Sweden periodical payments such as interest or annuities are allowed as deductions in computing

The practice in the United Kingdom is to make the person who pays interest or an annuity assessable to include the tax which he deducts when he makes the payments.

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the tax due from the person who makes the payments.

If Mr. X, out of his salary of £1,500, pays £300 a year under covenant to his widowed mother who resides elsewhere, this becomes income on which she pays the tax direct, and £300 is deducted from Mr. X's salary in arriving at his tax assessment. There are two assessments, one where Mr. X resides and the other where his mother resides.

Debenture interest paid by a company is excluded from the assessment on the company and is assessed to tax in the hands of the recipients at the places where they reside.

Government and other interest is also assessed directly on the recipients.

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The assessment of Mr. X would be on the full £1,500 and no assessment would be made on his mother. Instead of £300 he would pay her £300 less tax, and she would recover tax on her personal allowances from the Inland Revenue. There would be no tax to pay at the place where she resides.

In the United Kingdom the interest is included with the company's profits in one assessment and separate assessments are not made on the recipients.

In the United Kingdom the obligation to deduct tax is not universal but the exceptions are of limited scope.

Over a large field of taxation in the United Kingdom, income tax is not assessed and paid in the area to which it would need to be attributed if it were an alternative to local rates.

### *Basis of Computation of Income*

#### *(a) Employments*

The preliminary deduction of tax from salaries and wages is made by the employer on the basis of simple tables. There are only four classes of taxpayer and consequently only four columns applicable to each wage or salary group. There are separate tables for weekly, ten-day, fortnightly and monthly engagements. The Swedish system is very simple and is merely preliminary to an assessment in which credit is given for the preliminary tax deducted. The

The United Kingdom, with its more complex cumulative tables and its numerous codes, produces a closer approximation to the true liability. As a result it is possible for the administration to dispense with assessments in most cases. Other small items of untaxed income, interest, casual earnings, etc., can be dealt with by adjustment of the code number, and assessment of these extraneous items can be avoided. Where reduced rate on income taxed at the

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annual assessment can take care of any income other than wages and salaries, and the system permits of assessment in the commune in which the employee resides.

#### *(b) Profits from Trades, Professions, Etc.*

Company profits bear communal income tax and there is in addition a proportional national income tax of 40 per cent (now increased to 50 per cent) on company profits. This is not passed on to shareholders. Non-resident shareholders suffer a deduction in the form of a coupon tax (subject to the Double Taxation Conventions). Swedish shareholders pay both communal and national income taxes on any dividends from Swedish companies, and this results in an element of double taxation.

Much greater latitude is given in the computation of company profits in such matters as depreciation of plant, stock valuation, and reserves, than would be permitted in the United Kingdom.

This more generous attitude to the computation of corporate profits is not unconnected with the fact that in

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source is due, it can be disposed of in the same way, thus eliminating repayment claims.

There is no attempt to assess where the taxpayer lives. The deductions and payments are made by the employer for the whole of his employees at the business address, or in the case of an extensive business, for groups of employees at the place at which they are paid.

In the United Kingdom the tax on dividends is collected from the company as part of the assessment on its total profits. The dividends are not taxable in the hands of the shareholders, except to surtax (the additional income tax imposed in excess of £2,000 per annum). Exempt shareholders can recover from the Inland Revenue the tax deducted when they receive their dividends.

The underlying doctrine is that profits from trades and businesses carried on by companies are indistinguishable in nature from other forms of income and should bear an equal tax burden. The profits tax departs from this principle in singling out corporate income for special taxation, but it does not affect the status of company profits and income under the Income Tax Acts.

No allowances are given for amounts put to reserve or employed in strengthening the organisation. The United Kingdom has now a long tradition of heavy taxation of company profits, combined with the passing on to the shareholders of tax on their dividends by deduction.



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Sweden losses cannot be carried forward from one year to another, whereas in the United Kingdom losses may not only be carried forward but also in certain circumstances backwards and, in the case of groups under one control, sideways, from one company to another. It is in the general atmosphere of reasonableness between the companies and the tax administration in Sweden that fairly arbitrary methods of apportionment of the comparatively small communal income tax are widely accepted.

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#### *Company Taxation in Relation to Total Yield of Income Tax*

In 1953, companies and other bodies contributed only kr. 868 millions of the total receipts of kr. 3,783 millions from the state income tax and property tax combined.

Comparable figures are not available for the communal income tax, but the indication is that the proportion contributed by companies was even smaller.

The conclusion to be drawn is that company profits do not dominate the income tax in Sweden to the extent that they do in the United Kingdom.

In the United Kingdom for the year 1953-54 the total produce of the Income Tax was estimated at £1,682 millions. Tax under Schedule D amounted to £925 millions, of which £713 millions was assessed on companies, £120 millions on individuals, £61 millions on partnerships, £18 millions on local authorities and £12 millions on societies. In addition the profits tax on companies amounted to £303 millions (96th Report of the Commissioners of Inland Revenue). The total produce of the Income Tax in 1953-54 was £1,684 millions (Schedule D £1,006 millions, the profits tax £161 millions and Excess Profits Levy £89 millions).

#### *Initial Steps to Assessment*

The tax administration relies on the system of the national registration of the population.

The absence of deduction at the sources enables assessments to be made on all sources of personal income.

While there is a register for companies which is available to the tax administration, no register of individuals or firms exists. Reliance is placed on deduction at source, coupled with local sources of information supplemented by the distri-

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bution of information from the central office.

The system makes it unnecessary to devote much time to seeking out the individual taxpayer. If he is an employee he comes under PAYE. Farmers and property-owners are discovered through the rating lists. Traders and employers are traced through local channels.

Broadly speaking, the administration watches the source of income rather than the individual. Apart from employees, removals are followed up.

#### *Legal Liability to Make Returns without a Prior Request*

This applies to all residents in Sweden with incomes of kr. 1,200 and to non-residents who have earnings from Sweden of kr. 100 or whose assets in Sweden have a value exceeding kr. 50,000.

All persons having income which is chargeable with tax other than remuneration from employment, are legally liable to make returns.

#### *Returns of Husband and Wife*

Husband and wife make separate returns and where they are living together the family allowances are apportioned between them.

In law, husband and wife are regarded as one unit but, in practice, the earned income of the wife is separately assessed and carries separate allowances. Either spouse can, however, elect to make a separate return but this is not the normal practice.

#### *Change of Employment*

As employers deduct tax from the wages of a new employee at the rate laid down in the tax tables without regard to his previous earnings and tax, a change of employment without change of residence does not require any special action until the employee's return of the year's income is received in the tax office and his final tax is

Change of employment is dealt with by means of a certificate, P45, prepared by the employer. Two parts of this certificate are handed to the employee to ensure correct deduction by the new employer; the third part is absorbed in the administrative machine. In a straightforward case the new employer can make the

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computed. Where, in addition to the tax on wages deducted by the employer, the employee also pays tax on investment income, a change of employment without change of residence involves no re-assessment, but if there is a change of residence steps have to be taken by the tax office to transfer the liability to the new district as from the date of change.

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appropriate deduction without reference to the tax office.

The movements of employees are the major problem in a cumulative system. The number of "movements" is equal to 40 per cent of the total number of persons covered by PAYE. This would, however, exaggerate the incidence of movement, as some individuals would move more than once in the year.

### *Place of Assessment*

#### (1) *Employments*

Where the employee resided on 1st November preceding the assessment year.

Normally where the employment is carried on, or alternatively at the head office of the employer or where pay is issued.

#### (2) *Income from Real Property*

In general where the property is situated but only to the extent of the occupier's interest.

The occupier's interest is assessed where the property is situated, but normally this assessment also includes any rent and interest paid so that the income of other parties, e.g., ground landlord or mortgagee, is included in the one assessment.

Rents and interest on loans are deducted in arriving at income from property and these items of income are assessed in the commune where the recipient resides.

These charges on the property are not taxed where the recipient resides.

The position is complicated by the guaranteed income to the commune where the property is located of 4 per cent on the capital value.

The system is complicated in the case of owner occupiers who are also employees by the practice of using part of the personal allowances to cover the tax on the property, altering the PAYE code number to correspond. In such a case all the tax due is effectively charged on the earnings. This has obvious advantages for the employee and the tax machine, but it means that the point where the tax is



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### (3) *Income from Other Invested Capital*

In the commune of residence in all cases.

### (4) *Income from Trade, Business or Profession*

As explained in Chapter 4, some part of the profit is attributed to, and assessed at, all the permanent establishments of the trade, etc. Separate assessments are made in each commune concerned.

The question of what constitutes a permanent establishment can be troublesome. The trader, in preparing his return, need only apportion profits between the *läns*. The *lanstyrelsen* will make the division between communes but will expect the trader to supply the necessary data.

#### *Apportionment of Trade and Business Profits*

There are numerous bodies concerned with the splitting of profits. In the first place, the assessment boards of the districts (or communes)

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paid is remote from the place where the income arises.

Income from which tax is not deducted is assessed in the district of residence, but in the case of employees there may be a coding adjustment in lieu of assessment at the residence. This would be normal for small amounts of invested income.

Where the main income is from a trade, profession or farming, the assessment will be where the main income is assessed.

Where the tax has been deducted from the income at source, the assessment is made on the person or body paying the income and its location is determined by the payer's place of assessment—which will normally correspond with his residence or registered office.

The unit of assessment in the United Kingdom is the trade, business or profession. The whole profit is chargeable with tax at the place where the central management and control is located; there is no splitting. Apportionment between head office and mill, between factory and branches, or between manufacture and selling, is unnecessary.

In the United Kingdom a modified version of this problem of allocation of profits arises in the limited field where a company or concern which is

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where the trader or company carries on a business through a permanent establishment have to decide what profits should be attributed to the establishment concerned. The trader or company has to supply in his returns the information necessary for the apportionment. It is the duty of the Inter-Communal Appeal Board to control the decisions of the district boards. As each commune is obviously interested in securing the assessment of its due share of the income or profits, it is the practice, especially in the large cities, to invest a particular officer with the responsibility of taking care of the communal interests in this respect. This officer has certain rights of access to information in the trader's or company's return. The commune may appeal to the Appeal Board of the district concerned or to the Inter-Communal Appeal Board. Industrialists are not unhappy with this set-up. They have no objection to rule of thumb methods, particularly as the range of the communal rates of tax is not wide and the tax paid is allowed as a deduction in computing profits for the national tax.

The strain comes between the communes. The rural areas are dissatisfied. On representations from the *Landskommunernas Förbund*, the *Riksdag* decided in 1948 that this was an urgent problem, but nothing has yet been done. One of the difficulties is that rural areas have no staff with the training required for this work, nor have they the material on which to make satisfactory estimates.

Special rules are laid down for banking, other financial businesses, water, gas and electric power supply,

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non-resident carries on part of its trade in the United Kingdom. Common examples are the London branches of foreign or colonial banks. The branch is not a self-contained unit. Many of its transactions are initiated or completed outside the United Kingdom at the head office or at another branch. But as only the profit derived from trading within the United Kingdom is chargeable with British tax, it becomes necessary to measure the profit from parts of a series of transactions. There are various devices for getting round this difficulty. One is to split the global profit on the turnover basis, i.e., an approximation to the Swedish method. Another is to prepare a separate profit and loss account for the branch as though it were independent of its head office and sister branches. This involves splitting the results of individual transactions or splitting blocks of transactions of the same type. In general the administration would probably prefer the Swedish method (i.e., the splitting, on a rule of thumb basis, of the total profit of the undertaking) to the attempt to prepare separate accounts of the profits of individual branches, but the courts tend to lean in the other direction. They do not like rule of thumb methods. Their guiding principle was succinctly expressed by a famous Lord Chancellor, Lord Loreburn, in an income tax case in 1908 in the House of Lords: "A rule of thumb may be very desirable, but it cannot be substituted for the only rule of law that I know of, viz., that the true gains are to be ascertained as nearly as it can be done."

The ascertainment of the true gains

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railways, tramways, road transport services, canals, and other businesses.

A translation of the provision in the statute (Article 58 of the *Kommunalskattelag*) governing other businesses is as follows: "Businesses of a kind other than those dealt with specially (banking, railways, water, gas, electricity, etc.), five per cent, or, where circumstances require, a higher percentage [shall be assessed] in the commune where the head office is situated and in general in the communes where there are established places in which business is conducted, as can reasonably be taken having regard, within each commune, to the value of manufactured and processed goods, the magnitude of the turnover, the number of employed persons, and other circumstances which can serve as a basis for determination of the income which can be considered to have been earned within the commune."

Broadly speaking, where there is property belonging to, or occupied by, the trading organisation there will be a liability to tax if it can be argued that the operations give rise to any profit or accretion in value of stock in trade.

A note of the practice of the *Mellankommunala Prövningsnämnd* is given in Appendix III. All apportionments are on a rule of thumb basis, and special costing arrangements to determine departmental profits are rejected. It is only in the broadest sense that the communal tax is proportionate to the profits earned in a commune. After deducting a set percentage which is attributed to the head office establishment, the balance is normally spread arithmetically in

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of what is essentially only a part or section of a business gives rise to problems to which there is often no real solution. Such problems arise from time to time in the present tax system. They are always contentious and difficult. But at present they are only isolated problems and do not form an ever-present feature of the assessment of profits as would be the case if all trade profits had to be divided where it is necessary to attribute them to various permanent establishments.



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proportion to sales. When manufacture and sale are in different communes, there has to be a primary division of the overall profit between manufacture and sale. Each element may then require subdivision if, for example, successive manufacturing operations are carried on in different communes.

There are few appeals by the communes to the *Mellankommunala Prövningsnämnd* where divisions between provinces are handled. There are, however, separate offices in each *län* to deal with questions between the different communes in the *län*. We collected no data on the number of disputes or the amount of work involved in these offices.

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#### *Depreciation of Plant and Machinery*

The aggregate allowances are limited to the original cost of the asset, but considerable latitude has been allowed as to how and when the cost is written off for the purpose of tax.

Until 1950 traders could negotiate with the authorities an almost immediate writing off of the total cost, but this privilege has since been modified. The upper limit since 1952 has been 20 per cent of the first cost, but there is a recommendation of a government committee, not yet implemented, that optionally 30 per cent on written down value should be allowed.

The position from 1950 to 1952 is a little obscure. Reinvestment in capital assets was conducing to inflation, and a special tax of 10 per cent for each of two years was imposed in certain circumstances on new expen-

Normal allowances are on a written-down basis calculated so as to reduce the cost to break-up value over the useful life of the asset. There has been nothing comparable to the free writing-off permitted in Sweden up to 1950.

Types of plant are classified and appropriate rates of allowance calculated. These allowances are given after the assessable profit has been computed. Since 1946, with the exception of the period from April 1952 to April 1953, there has also been given an initial allowance at rates fixed in the Annual Finance Acts for all new expenditure on plant, machinery and industrial buildings. From April 1954, a further inducement to capital investment has been given in the form of an investment allowance which will permit, over the whole life of an asset, aggregate

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diture. This ceased and was followed by a year in which 12 per cent was assessed on new assets, but only in large cases, and related to the difference between the writing-off claimed and the normal allowance. The system seems to have been rather flexible.

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allowances exceeding the original cost.

#### *Treatment of Stock in Trade*

In keeping with the free treatment of capital assets, industry was permitted, prior to 1950, to write down the value of stock in trade below market value, with the effect that the realised profit on goods sold was diminished by a fictitious notional loss on goods still held. This practice deferred the payment of tax on the true profit and conduced to the purchase of excessive quantities of stock. The limiting figure was 30 per cent of cost below which the valuation was not allowed to go, but obviously a writing down of stock by 70 per cent produced a major distortion of the accounts.

A government-appointed committee which considered this matter suggested an increase from 30 to 50 per cent but this recommendation has not yet been put into effect. The justification for heavy writing down of industrial stock in trade is said to be that it permits the building up of internal reserves and the strengthening of the economy to meet a possible trade depression.

There is no comparable practice in the United Kingdom. Stock in trade may be valued at cost or market price, whichever is the lower. Where prices are falling this means that the realised profit on the goods sold is diminished by the potential loss on the goods in stock, this being the difference between their cost and their value at balance sheet date. There is no creation of a hidden reserve against prospective loss in excess of the loss which is already reflected in the fall in prices.

#### *Loss Incurred in Trade or Business*

This is deductible from any profit in the same year falling within the same tax category. Losses, however, may not be carried forward or backward to be set against profits of other

There are several options open to the taxpayer. The effect of these is that an unrelieved loss is now very rare. The income relieved by setting off the loss may be the income of the

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years. If it were not for the free treatment of stocks and capital assets, this would be a heavy price to pay for the annual ascertainment of profit. Capital losses are not, in any event, deductible.

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same or the following year from some other source; the income assessed on the same trade for the current or succeeding years without time limit; or, if the loss arose in the last year of a business, the income from that business in the preceding three years.

Capital losses on the disposal or scrapping of industrial buildings, plant or machinery are allowable under the designation of balancing allowances. Other capital losses are in general not deductible.

### *Capital Profits and Casual Profits*

A brief description of the basis of the tax on capital profits is given in Chapter 4. There is a set-off for losses incurred in the same year in similar transactions. It has a deterrent rather than a profitable effect, the actual yield being very small.

Moreover there are, no doubt, certain social advantages in drawing the net so widely.

Capital profits are not taxed in the United Kingdom unless they recur in such a manner that the transactions merge into a trade or business, the ultimate profit or loss being the profit of the trade or business and not of the individual transactions. The fact that this allows a number of fortuitous gains to escape tax which might on a wider definition of income be thought to form a most suitable subject for taxation, has attracted much comment in recent years and will no doubt receive the attention of the Royal Commission which is at present sitting.

### *Collection of Tax*

Preliminary tax is a form of payment on account based broadly on the method of self-assessment but with a more immediate official scrutiny of the return than is customary under some systems. The officials issue demand notices for the preliminary tax and deal with disputes as to the amount to be paid. There is the difficulty, usual in the case of trade

Tax on many forms of income is automatically deducted at standard rate, leaving the adjustments for family allowances and reduced rate to be made on other assessments or, failing that, by an annual repayment claim.

Collection in regard to employments is through the employer.

In the case of trade profits, the



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profits, of determining in advance of the completion of accounts what is a fair profit on which to pay on account. Interest is payable in certain circumstances on underpayments and also at a lower rate by the Crown on overpayments. Much official time is taken up by matters relating to preliminary tax.

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basis is normally business completed before the year of assessment begins, but the time taken by the preparation of accounts and the agreement of liabilities often extends beyond the date when the tax is due. In important cases payments on account are collected usually by informal negotiation, but with legal sanctions in the background.

Interest does not begin to run until the liability is determined and plays an insignificant part in the tax administration. No interest is paid by the Crown on overpayments.

## Chapter 9

# THE EFFECT OF THE DIFFERENCES BETWEEN SWEDEN AND THE UNITED KINGDOM ON THE POSSIBLE INTRODUCTION OF A SYSTEM OF LOCAL INCOME TAX IN THE UNITED KINGDOM

IN this chapter we consider the effect that the differences between Sweden and the United Kingdom would have on the possible introduction of a local income tax in the United Kingdom.

### TRADE PROFITS

In most cases the location of income from trade can be determined in Sweden without much difficulty. Our only doubts on this score are concerned with the method of apportioning the profits of a trade or business which has a footing in more than one commune. This appeared to us to be rather arbitrary in its effect and to be almost unworkable in the conditions which prevail in the United Kingdom.

Our opinion rests on two factors. The first is concerned with the different physical conditions under which much of the trade and manufacture of the United Kingdom is carried on. Separate rating authorities are contiguous in industrial areas, goods and services move freely across the boundaries of the cities and towns, and taxation does not hinder the dispersal of the manufacturing processes of a concern over a number of factories in different areas. Such conurbations as Birmingham and the Black Country, and parts of the West Riding of Yorkshire or Tyneside, have no counterpart in Sweden.

Sweden has only eleven towns and cities of more than 50,000 inhabitants and they are widely separated. There are no large towns adjacent to one another, and inevitably the processes of manufacture and trade must be more concentrated than in the United Kingdom. Moreover, this tendency is encouraged by the severity of the Scandinavian winter and the consequent difficulties of road transport.

The major strain in the division of profits in Sweden is between rural and urban areas. In the United Kingdom a similar system would, however, set our urban areas at loggerheads with one another to a far greater extent.

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The second factor turns on the existence in the United Kingdom of a body of experts in taxation on whose advice industry is prone to act. We formed the conclusion that claims are pursued in a more determined manner here, and that decisions of the administration are not so readily accepted as in Sweden. If this impression is well founded, it would add to the difficulty of working a system on the Swedish pattern which depends, so far as the allocation of profits is concerned, largely on rule of thumb.

The apparent willingness of Swedish industry to accept the official apportionment of profits often has its origin in local conditions. Many an undertaking having a big establishment in a remote commune with a high rate of tax does not see much point in trying to get a larger proportion of its profit attributed to its establishments in other areas because its own organisation and the welfare of its own staff often account for the greater part of the cost of the services of the highly taxed commune. In other words, if it is the only large concern in the commune it is of little consequence whether it pays a low communal rate on a high profit or a high communal rate on a low profit, if its contribution has to provide the major part of the communal revenues.

### INDIVIDUAL INCOMES

The Swedish system is based on direct assessment of the individual, and he can without difficulty be charged with tax on his whole income in the district in which he lives. The bulk of the total tax yield is derived from assessments on personal incomes, and such difficulties as arise in other fields do not seriously embarrass the local authorities. There is no deduction at source from dividends and interest. Such types of income are thus assessable in the commune of residence, and the basic principle of the communal income tax is satisfied without any strain on the administration. To arrive at a similar result in the United Kingdom, it would be necessary to set up new machinery to apportion to the communes of residence the tax collected by the employers, but this would only cope with the simple problem of a uniform rate. We are unable to visualise any workable system under which employers could be held responsible for deducting at different rates according to the place of residence and which would at the same time maintain the cumulative principle.

A similar difficulty exists on a smaller scale in regard to dividends and taxed interest.

There is a large field of employees whose total income is insufficient to bring any part of their income into standard rate taxation: single



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persons with earned incomes up to, say, £10 a week and investment income of, say, £100 a year; married men with children and substantially higher total incomes. In these cases the coding system takes care of the difference between any standard rate tax which has been deducted and the reduced rate of tax due from the recipient. Similarly, if the investment income has been received in full (e.g., bank interest or interest on Defence Bonds), the coding system takes care of the tax on this income at the rate appropriate to the recipient's total income. It is difficult to see how the coding system could be modified to take account of a flat rate of communal tax variable according to the locality of residence, and of a rate of national tax varying with total income. Conceivably dual codes might be framed, but it is doubtful whether the system would be workable and would be understood by employees and employers. It would be an administrative nightmare.

## NEED FOR NATIONAL REGISTRATION

The tax machine in Sweden gets into gear each year with the preparation by the census clerk (in towns by the *kronokamrerare*) of a register of persons liable to make returns in each commune. He is in a position to do this because of the continuous registration of the population with which he is entrusted. In rural areas the responsibility for registration is shared with the pastor of the church. Every person is taxable according to the place at which he was registered as a resident on 1st November of the year preceding the fiscal year.

Some such arbitrary basis of localisation is essential in a system where all income has to be localised.

It is important to realise what registration involves. Every person entered in a parish register has to be recorded in the County Registry Office or the National Registry Office and is allotted a birth number—odds for males and evens for females—which, together with the date of birth, constitutes a record of identity. Every person has to be registered in his parish of residence and every change of residence involves a change of registration. Every registered person over fifteen years of age has a card issued to him by the County Registry Office giving his name, date of birth, birth number and parish registration district. This is the citizen's card or the alien's card.

A person from another country becoming a Swedish resident must, within fourteen days of taking up his abode, register in the parish in which he lives. Any person leaving to take up permanent residence abroad must first apply to the pastor of the parish in which he is registered for an emigration certificate.

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A census is held annually in every census district, the name of every person who will be recorded in a parish register in the country on the 1st November of the census year being entered on the census return. Each county council is responsible for national registration in the county and has to keep a list of birth numbers, an address register and a number register. The Central Statistical Bureau is the central body responsible for administering and supervising the national registration system throughout the country. Husbands and wives are dealt with independently of one another.

If, in order to introduce local income tax into the United Kingdom, it were found necessary to switch the point of approach from the source of income to the person of the taxpayer and to make him the unit on which the administration operates, it might be found necessary to use some form of national register as the foundation. One could visualise much opposition to such a step.

### DISPENSING WITH ANNUAL ASSESSMENTS

It is one of the merits of the cumulative nature of the British PAYE system that it removes the inequalities that arise in an arrangement under which each week is treated independently. In the independent system employed in Sweden, if the weekly rates are fixed so as to give the correct annual total when earnings are consistent over the whole year, over-deductions arise when earnings fluctuate. For example, it is possible for a man working a long week and a short week alternately to have tax deducted in each of the long weeks but not to be liable to tax at all for the year taken as a whole.

In the cumulative system, the tables are so arranged that in the first week of the year the employee has  $1/52$ nd of his allowances for the year set against his pay; in the first two weeks he receives  $2/52$ nds against the total of his first two weeks' pay; in the third week  $3/52$ nds against the total of his first three weeks' pay; and so on throughout the year. He also receives a growing amount of earned income relief and reduced rate relief. In this way the total tax deducted up to any given date is kept in line with the total pay to date. If wages fall, the tax deduction falls too; and if the fall in wages is sufficient there may be a repayment due.

The nature of this system has a bearing on the making of assessments after the end of the year. The approximations in the system of "code numbers" and in the tax tables give rise in most cases to small under-deductions of tax, even where the code number has been correct and the system has been correctly operated by the

employer. To make assessments in all these cases would involve a great deal of work for very small results, and it was consequently provided by the Finance Act, 1948, that an assessment need not be made where an under-deduction arose solely because of the approximations in the system.

As a result, personal assessments need only be made on one-fifth of the total number of employees. The employer's responsibility is completed by paying over the tax deducted in accordance with the tables and by returning the tax deduction cards with a certificate of the total remuneration. Apart from routine checking, no further administrative steps are required in four-fifths of the cases.

To revert to a system of annual assessment in all cases, with balances to be collected or repaid, would involve a formidable addition to the work. If it was accompanied by a reduction in the exemption limit, to ensure wider dispersal (as in Sweden) of the burden of the cost of local services, the position would be aggravated.

The close approximation to the tax deducted under the cumulative PAYE system to the true liability enables annual returns to be eliminated in so large a proportion of cases that the system becomes administratively manageable. It was explained in the previous section that, of 20½ million personal incomes above the exemption limit, only about 12½ millions make returns each year. As compared with the requirement under a communal income tax, of a precise determination of total income in all cases, there is, even within that total of 12½ millions, a preponderance of taxpayers for which it is unnecessary to calculate total income. The range £500 to £2,000 comprises 4,680,000 individuals, who account for about 3½ of the 12½ millions who make returns. In the bulk of these cases, if they have taxed income other than their pay or trade and professional income it would normally be unnecessary at present to make a precise calculation of such income because the latter would not affect the amount of their assessments. Small omissions or inaccuracies of taxed income do not need to be corrected.

If an annual return is regarded as a *sine qua non* of a communal income tax, in addition to bringing in a substantial part of the 4 million individuals over the exemption limit who are at present wholly relieved from tax by allowances, returns of total income would also be required from an additional 8 millions who, though liable, are not at present served with forms. Moreover, a higher degree of accuracy and checking would be required in all cases where, under the present system, a computation of total income is not material.

This affords an indication of the magnitude of the task, supposing



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that some method of overcoming the difficulty about location of income could be devised.

### DOUBLE TAXATION AGREEMENTS

The effect of the introduction of a local income tax on the double taxation agreements to which the United Kingdom is a party, would also require careful consideration. There are sixty-seven of these agreements.

In some agreements to which she is a party, Sweden has been willing to concede exemption from communal income tax, but not in others. The United Kingdom does not give tax credit for Swedish communal income tax, nor for the similar communal income taxes in Denmark and Finland. On the other hand, the Norwegian communal income tax and communal surtax are brought into the Anglo-Norwegian agreement on special terms, which provide that credit may not exceed one-half of the Norwegian tax (proviso to Article XVI(i) of the agreement).

The difficulty which the double taxation agreements to which the United Kingdom is a party, import into any proposal to introduce a local income tax in the United Kingdom arises out of the over-riding sub-clause which usually follows the definition of included taxes and which reads as follows:

*Anglo-Norwegian  
Agreement*

Art. I 2. The present Convention shall also apply to any other taxes of a substantially similar character imposed in Norway or the United Kingdom subsequently to the date of signature of the present Convention.

*Anglo-Swedish  
Agreement*

Art. I 2. The present Convention shall also apply to any other taxes of a substantially similar character imposed in the United Kingdom or Sweden subsequently to the date of signature of the present Convention.

If a local income tax was imposed in the United Kingdom, the existing double taxation conventions would divide themselves into three classes:

1. The Anglo-Norwegian agreement, under which the new tax would qualify for relief under Article I 2 as being of a substantially similar character to a tax cited in Article I 1.
2. The Anglo-Swedish, Anglo-Danish and Anglo-Finnish agreements, where both contracting parties would have similar communal income taxes outside the scope of the present agreements.

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### 3. Agreements with other countries which have no comparable local income taxes.

As regards 1, there was presumably no intention on the part of the United Kingdom to give exemption to Norwegians in respect of local rates levied in the United Kingdom, and if the effect of the changeover to a local income tax means that exemption will then be due, a re-negotiation of the agreement may well be sought by the United Kingdom. The initiative in the second group might come from either side. A new factor, in the shape of a new tax on income, will have been introduced by one party to each of these agreements. According to the direction of the balance of advantage, so may rest the initiative in asking for revision. In the third and largest group, there should not be much difficulty unless some benefit is obtained by signators in the first two groups, but it is unlikely that there would be no repercussions to so important a change in the United Kingdom tax system.

The agreements covering air transport and shipping are simpler in form than the general agreements, and the matters mentioned in this section do not give rise to any exceptional problems in relation to them. The profits are taxed by the country in which the enterprise is resident and exempted from tax elsewhere.

## Chapter 10

### THE TREND OF PUBLIC OPINION IN SWEDEN ON THE TAXATION SYSTEM

Our discussions were mainly with officials of the state, the municipalities and the various associations of local authorities. We found that opinion on the incidence of direct taxes tended to follow political lines of cleavage. In consequence, officials were as a rule non-committal. Our stay was not long enough for us to interview a full cross-section of the people, but criticism, as might be expected, tended to concentrate on the weight of taxes in total, particularly in regard to the middle classes.

We found no evidence of hostility to the system of registration. We formed the impression of a wide popular awareness of Sweden as a small nation, not militarily strong, living in close proximity to larger and more powerful neighbours. Obligations such as registration which the state thinks necessary for national survival are not critically regarded. The Swedish industrial revolution is comparatively recent, and there is less concentration of industry in large units than in the United Kingdom. In recent years there has been a rapid advance in living standards, in particular among the lower income ranges, and this has conduced to industrial peace and a willingness to accept the system of taxation and local government without serious criticism. National registration is accepted as an inherent part of the system.

Income, as a measure of ability to pay, seems to be generally accepted in Sweden as a suitable basis for local taxation. Criticisms are confined to matters of detail, such as the apportionment of business profits. There is a tendency in Sweden to have regard to taxation as a whole and not to think separately about the communal income tax. The more vocal sections of the nation are concerned mainly with the weight and incidence of the state tax, and criticisms run on lines familiar in this country.

It was suggested to us that the mass of unpaid public work done by members of the assessment and appeal boards helps to link the public-spirited part of the community with the administration and tends to damp down criticism. It has created a body of informed opinion on the difficulties of tax administration.



Points to which particular criticism was directed were:

1. The heavy incidence of the communal tax on the lower income ranges, particularly on workers with large families. The criticisms of the incidence of the tax tended to cancel one another. Some officials saw no reason why the family man should pay less than the single man.
2. The rather ungenerous treatment of the working mother, whose special allowance falls far short of the cost of engaging domestic help.
3. The variation in rate of tax as between one residential area and another.
4. The absence of uniformity in practice between one office and another.
5. The inadequacy of the taxation inducement to saving. The opinion is widely held in Stockholm that the rate of private savings is too low.

We were somewhat surprised that the treatment of company profits evoked so little criticism. We were told that the trade unions do not display any hostility to the creation of untaxed reserves. This was explained as due to their acceptance of the view that the accumulation of reserves and the ploughing back of profits are vital to a healthy economy, and that workers and proprietors in an industry both benefit when its finances are managed with expansion as a major motive.

On the question of apportioning profits, the rural areas would like a larger share attributed to them. Some officials in the urban areas think the rural communes get too much. The administration uses so many measuring devices—sales, fixed capital, wages, management may each have a part to play in the apportionment—that there is ample scope for argument as to what relative importance attaches to each factor in regard to each undertaking.

Criticism of the administration for not doing more to combat evasion was evident in some quarters. There is a good deal of public restlessness, but this again was concerned mainly with the state tax. No particular reference was made to evasion of communal income tax, except in reference to the small vagrant population, who are a problem with all types of direct taxation.

No doubt the registration system helps to keep down the number of untraced taxpayers, but we heard some surprisingly high estimates of the losses from understatement of incomes. In the absence of authentic information these can be little more than guesses.

## Chapter II

### DIFFERENCES IN INCIDENCE BETWEEN A RATING AND AN INCOME TAX SYSTEM AND EFFECT ON DISTRIBUTION OF YIELD

THE object of this chapter is to compare the incidence of a local income tax with that of a rating system such as we know in this country, and to consider the effect that the introduction of a local income tax would have on the distribution of the yield as between different local authorities.

When any sweeping change in taxation is under consideration, changes in the incidence of the burden are of vital importance, not only from the social but also from the political aspect. Our study of the Swedish system has made it apparent that one of the effects of introducing a similar system into the United Kingdom would be a major revolution in the way in which the cost of providing local services is apportioned among the inhabitants.

#### LEVEL OF PRICES, WAGES AND SALARIES

In order to assess the effect of the change in the incidence of the tax, it is necessary to compare what would be the burden of tax under each system on people in various income ranges. A direct comparison based on Swedish income statistics might be misleading if there were any substantial differences between the two countries in the levels of prices or wages. We were not able to make a full statistical survey but we learnt enough to indicate that the current rate of exchange (kr. 14.53 to the £) does not give an accurate measure of the relative purchasing powers of the two currencies. Where prices in the United Kingdom are appreciably inflated by purchase tax, it is occasionally possible to buy more cheaply in Sweden, but where purchase tax is absent, and even in some cases where it is not, the British prices are appreciably lower.

Rents in Stockholm working-class areas tend to be higher than for comparable houses let by local authorities in the United Kingdom, but larger properties, e.g., flats with lifts and heating, are not dearer in Sweden than in the United Kingdom. Clothing in Sweden is a little dearer, and so is short-distance travel. Food also seemed to be

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a little higher in price. On the whole we felt it would not be unreasonable to regard Swedish prices on average as 10 per cent above those in Britain.

As to wages and salaries, most of our time was spent in Stockholm and there we found the wages of manual workers higher than in, say, London. The basic wage for a lorry driver is kr. 169 a week and for a labourer kr. 166; converted to sterling this represents £11 13s. od. and £11 9s. od. respectively. In country areas wages are lower, but not to such an extent that they approach the United Kingdom level. A police constable and a fireman employed by the Uppsala Town Council earned respectively kr. 11,270 and kr. 10,692 per annum, equivalent in British currency to £777 and £737 respectively.

The comparative level of salaries is less easy to determine. Using the official exchange rate, the emoluments of the chief officers of a town council seem to compare reasonably with those of corresponding officers in the United Kingdom. The disparity prevalent in the lower income groups tends to disappear at higher levels. The salary and allowances of the chief tax official of Uppsala are equivalent to the remuneration of a senior tax inspector in a town in England or Scotland of comparable size. With regard to still higher salary ranges, e.g., the general managers of industrial corporations, railways, banks, etc., we collected no specific information, but the national statistics of incomes of all types published in both Sweden and the United Kingdom provide a basis for comparison. From these statistics we were able to draw the conclusion that in the ranges above £2,000 per annum the salaries paid in Sweden are lower than for similar positions in the United Kingdom.

A comparison on a national basis can also be made statistically for all wages and salaries. This shows that, at the official rate of exchange, the average Swedish income falls short of the average United Kingdom income by about 12 per cent. We came to the conclusion, therefore, that in comparing income levels in the two countries it would be reasonable to convert the kroner at 16 to the £ against the official rate of 14.5—a difference of approximately 10 per cent.

#### INCOMES CLASSIFIED BY RANGES

In Appendix I, Table 7, we give the Swedish official figures for the distribution of incomes in income ranges. In Table 8 the corresponding figures are given for the United Kingdom. By re-arranging the Swedish figures, and working on the rate of exchange of kr. 16 to the £, which we have suggested above, it is possible to produce a distribution of incomes for Sweden which can be compared directly



with those for the United Kingdom. These figures are also given in Table 8. The results bear out what has already been written about the relativity between Swedish and United Kingdom incomes. Up to £250 per annum the figures are virtually equal, 19.78 per cent for the United Kingdom and 20.11 per cent for Sweden. Above that figure disparities appear. 50.62 per cent of all United Kingdom incomes fall within the range £250—£500, but in Sweden only 39.41 per cent. This is counterbalanced in the ranges £500—£750 and £750—£1,000 by a swing in the reverse direction which continues to the £2,000 level, when a swing back begins and continues to the highest limit. The Swedish incomes between £500 and £2,000 number 39.73 per cent of the total, as compared with 28.34 per cent in the United Kingdom. The Swedish excess between these ranges counterbalances an excess of incomes between £250 and £500 in the United Kingdom of 11.21 per cent as compared with Sweden. The percentage of incomes over £2,000 in the United Kingdom is almost double the comparable figure for Sweden. The Swedish figures are for the calendar year 1952, those of the United Kingdom for the year ended March, 1952.

#### EFFECT OF DISPERSION OF INCOMES ON INCIDENCE

Having arrived at a broad comparison of the spread of incomes in the two countries, we begin to see that certain adaptations of the incidence of a communal income tax might be necessary in a country where conditions differ from those in Sweden. In a community such as Sweden, with a more even distribution of incomes, the flat-rate family allowance has less effect on the proportional character of the tax than it would have where there are more poor, more rich, and fewer in the middle ranges. Assuming exempt family allowances not lower than they are in Sweden, the change of incidence from rating to income tax for a household with two or more income-earners would normally be less acute in the United Kingdom for the majority in the lower income ranges, because the ratio of exempt allowance to chargeable income would tend to be higher.

One could discuss the hypothetical effects of different levels of exemption at great length, and this forms a very important element in the incidence of any scheme of local income tax. As we have pointed out in Chapter 6, there are many factors which prevent a straight comparison of incidence between Sweden and the United Kingdom. The columnar statement in Appendix I, Table 9, gives only a partial picture, but we have not thought it advisable in this report to attempt an evaluation of the various distortions which exist.

## INCIDENCE UNDER A RATING AND AN INCOME TAX SYSTEM

### CHANGE IN DISTRIBUTION OF YIELD

With the exception of the year 1951-52, when the report of the Commissioners of Inland Revenue included an analysis of incomes by counties, separate figures are given only for the three areas of England and Wales, Scotland and Northern Ireland. There is no means by which the county figures can be divided into urban and rural areas, and we are unable to offer any statistical basis on which to calculate changes of incidence area by area. It does seem evident, however, that there would be a considerable change in the tax base, of which the chief benefit would go to urban areas.

The return of *Rates Levied per Head of Population (England and Wales)* 1954-55, compiled by the Institute of Municipal Treasurers and Accountants, shows in Part II the net rate per head for all county boroughs, metropolitan boroughs and a representative selection of non-county boroughs, urban district councils and rural district councils. Adjoining rating authorities show wide variations. The U.D.C.s of Friern Barnet and Barnet levy 212/5d. and 277/7d. per head respectively; Potters Bar, which is contiguous to Barnet, 247/11d.; and the Rural District of Hatfield, immediately to the north of Potters Bar, 203/3d. No wide disparity of personal incomes in the areas of these authorities seems likely, and it is interesting to study the effect of adding to the tax base of the Hatfield area a big slice of the earnings of the De Haviland Aircraft Company, which has its headquarters and part of its manufacturing organisation there. The consolidated profit and loss account of the De Haviland group of companies for the year ended 30th September, 1953, disclosed a profit, before deducting taxation, of more than £2½ millions. There is no organisation of this magnitude in Barnet or Potters Bar. The rateable value of Hatfield at 1st April, 1954, was £217,232. It would be an interesting subject for further study to try to analyse for these rating authorities the effects of a communal income tax on the Swedish pattern. We cannot do more in this report than draw attention to the resultant variations in distribution of the yield, and suggest that many secondary problems would arise.

### ESTIMATE OF AVERAGE RATE OF LOCAL INCOME TAX NECESSARY IN UNITED KINGDOM

It is possible from the available statistics to compute the probable average rate of communal income tax over the whole country which would be necessary to produce the equivalent of the present rating revenue. The true net income of the United Kingdom as shown by

the income tax assessments (all schedules) made in 1951-52 was £11,061 millions. If we assume an average family allowance of £150 per head for 20½ million income earners (the Swedish figure is substantially lower than £150), we should have to deduct £3,000 millions, leaving the communal rate to be levied on £8,000 millions. There would be some variations between the national and the communal tax base, as there are organisations which are exempt as charities from national tax but which would be brought into a communal tax. These differences would not be sufficiently large to affect the general picture. There would still be profits and income of the order of £8,000 millions to produce the required rate income of £318,087,000\* for England and Wales and £36,744,000 for Scotland, a total of £354,831,000 plus a modest amount for Northern Ireland. An average rate of 4.5 per cent or 11d. in the £ would suffice. On a flat rate basis, some £76 millions would be the share falling on corporate profits.

The figure of £76 millions probably overstates the levy on industry owing to the probability that in areas of great industrial establishments the rate of communal income tax would, by virtue of the effect of their presence in the local tax base, be much lower than the national average. Correspondingly, of course, purely residential areas would need to levy a higher rate.

If the Swedish model were followed, all local income tax paid would be a deduction from income for national tax. The loss to the Exchequer at current rates of income tax and surtax in respect of personal incomes would be considerable, but it is difficult from the available statistics to make a close estimate. We estimated, however, that the maximum figure would be in the region of £110 millions but, as in arriving at this figure all assumptions were made on a basis which tended to inflate the result, it seems probable that the real loss would fall somewhere in the range of £60 to £70 millions.

To this we must add the appropriate adjustment for corporate incomes. We have shown that local tax on corporate profits would be something less than £76 millions, but how much less we cannot say. We have therefore taken the £76 millions less the rates at present paid by corporate bodies as the measure of the prospective reduction in profits assessable to the national tax. The rateable value of all commercial and industrial buildings is given as £82 millions (in

\* The figures are increasing, the 1952/53 figures for England and Wales being £335,869,000, exclusive of the BTC and CEA payments in lieu of rates (White Paper on *Local Government Financial Statistics 1952/53*) but the available taxable income is also increasing and no great variation in the ratio need be anticipated.



Chapter III of the main report). This should be assumed to be divided between corporate bodies and other occupiers in the ratio which the trading income of companies bears to the total trading income. On this basis, the share of corporate bodies (which also includes such local authorities as make profits from trade) would be about 63 per cent, which attributes to corporate bodies the occupation of commercial and industrial buildings of a rateable value of £51.6 millions. Taking the average rate poundage as 20/1d. (1952-53), this means that a local tax on corporate profits would produce £76 millions, as compared with £51.8 millions paid in local rates. The resulting loss in national income tax would be approximately £10.9 millions (£24.2 millions at 9s. in the £). The diminution in profits tax would be too small to affect the budgetary balance.

In total, therefore, the Chancellor of the Exchequer might be faced with a drop in revenue of the order of £80 millions. In a time of rising revenue, a deficiency of this order might well be absorbed without any increase in direct taxes, though the possibility of some rearrangement of the national tax burden cannot be ruled out. In considering the variation of incidence on individual taxpayers, we do not adjust the figures to take any such possibility into account.

#### VARIATION OF INCIDENCE ON INDIVIDUALS

We have no alternative but to work on an average local income tax rate for the whole country, and to compare this with the average burden of rates at the present time.

In Appendix I, Table 9, there is a comparison of the present total rate and tax burden at different income levels in Sweden and the United Kingdom. An additional Table 10 has been prepared, in which the present United Kingdom rate and tax burden is compared with the burden of a local income tax at 4.5 per cent on the excess of income over £150 per annum, with the allowance of the local tax in computing national tax income. Two further columns for non-householders are added. This class comprises at least one-third of the income receivers. To them the imposition of a local income tax is a total loss, there being no direct mitigation in relief from rates.

These figures are put forward with every reserve and should be read as indicators rather than mature assessments. Other variable factors enter into each case: differing family circumstances, variations from average rating or average standard of housing, and the local variations in the rate of local income tax already referred to. There will be few taxpayers who are not affected by two or three factors,

and the ultimate outcome for any individual is uncertain. Moreover, these figures only take into account the rates paid in the capacity of a householder, and do not make allowance, where the income is derived from trade or business, for any rates paid on business properties. This factor would cause some distortion, and although national statistics have been used to arrive at the average rate of local income tax, the comparisons in Tables 9 and 10 relate only to wages and salaries.

With these reservations, it still remains possible to draw some useful conclusions from the figures. The first is that a married householder, living in a house appropriate to his income in a district where the level of rating and the substituted local income tax approximate to the national average, would find his total tax burden much the same as at present. The point at which the exemption limit for local tax has been drawn in these calculations means more relief in the higher ranges and no relief for those under £500, but this would be adjusted if the exemption limit were raised to £200 or £220. Such a limit would not create a large class of beneficiaries from local services who do not contribute to the cost, a danger referred to in Chapter 6 as a possibility if the exemption limit for local income tax was pitched too high.

The non-householder under the proposed scheme would contribute substantially more at all stages than he does at present.

The great disparities will probably arise as between one area and another, but without further research these cannot be quantified.

It may be said that in one sense the changed pattern of taxation would not perpetuate the regressive nature of the present rating system. The anticipated local tax would work out at 3.2 per cent on an income of £500 and 4.4 per cent on an income of £10,000, but as the change would be accompanied by relief from national tax to the extent of nearly 4 per cent on the £10,000 income as compared with 0.6 per cent on the £500, the regressive element still remains as an element in total tax, although concealed by the way in which the new tax would be computed. This again focuses attention on the point which was made in Chapter 7, that it is not easy to see on what grounds Sweden decided that the local tax should be a deduction from income for national tax purposes.

#### VARIATION OF INCIDENCE ON COMPANIES

It had been intended to prepare a statement showing the effects on companies at different levels of profit, but this proved impossible as there is no relativity between present rating and company profits. In the case of householders, one can assume that higher incomes go

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with larger houses and higher rates, but this assumption would break down in the case of industrial and commercial activities. The question of how individual companies would be affected by the change of basis is very complex and would need a great deal of study before any conclusions could be formed. We have already pointed out that the additional burden on corporate industry and commerce might well be in the region of £24 millions, and it is interesting to see how this compares with the figure of £50 millions<sup>1</sup> which would be the addition to local rates if industrial derating were abolished.

## VARIATION OF INCIDENCE ON INDIVIDUALS AND PARTNERSHIPS ENGAGED IN TRADE, COMMERCE AND FARMING

The change in incidence on farmers would not differ materially from that on wage- and salary-earners, for agricultural land and the accompanying buildings are already relieved of rates. In England and Wales, the farmhouse has a special basis of valuation under Section 72 of the Local Government Act, 1929, and to that extent perhaps the comparison between present taxation and the local income tax scheme would not be quite so favourable for farmers as for employees on the same income level, but the differences would be slight.

All individuals and partnerships in trade and commerce would enjoy an improved position under a scheme on the Swedish pattern. We have estimated the possible additional cost to corporate industry as £24 millions less £10.9 millions relief from national tax, a net loss in round figures of £13 millions. The Exchequer would also lose a sum in the region of £80 millions. As to employees, there is a small gain for householders and a rather larger loss for non-householders. If these figures are reasonably accurate, there must therefore be a substantial gain to the other large section of the community.

Individuals and partnerships engaged in trade and farming number approximately 1½ millions, of whom 384,000 are farmers and horticulturalists. The true net income involved is £914.8 millions. Deducting the income from farming (£149.8 millions) we are left with a net figure of £764.5 millions for traders and businesses other than farming (*Inland Revenue Report* for 1952-53). The owners of such businesses will approximately break even in their personal capacities, in line with the figures worked out for different income levels in Appendix I, Table 10, but they will be beneficiaries in their capacity as traders, being relieved of local rates on their business premises.

In apportioning to this class only 37 per cent of the total rate burden

<sup>1</sup> This figure was estimated before the revaluation of 1956.



on industry and commerce, it seems likely that we have underestimated their true share and have not given sufficient weight to the effect of derating in relieving corporate, as compared with individual, undertakings. It may well be that the latter are at present bearing a much larger share than 37 per cent of the rates on the £82 million rateable value of all commercial and industrial premises.

#### CONCLUSIONS

There is too much approximation in these calculations of the relative burdens of rates and taxes for us to achieve an equation on a national basis, but certain definite conclusions are justifiable.

The group of ratepayers which would gain most from a changeover from rates to income tax would be individuals and partnerships engaged in trade. While employees in the aggregate would probably retain an approximate equality with their present position, there would be changes for classes, such as non-householders, who would have more to pay, and for the lowest income levels, whose relative gain or loss could be adjusted by raising or lowering the exemption level. The chief sufferers would be the national exchequer and corporate industry in the aggregate. The effect on corporate industry would vary considerably from area to area.

As regards farmers, the general conclusion is that they would suffer by losing the benefit of the special valuation for farmhouses, and if this surmise is correct, the proposed change might prove helpful to predominantly rural rating authorities. The chief beneficiaries among the rating authorities would, under present conditions, be the highly industrialised areas, and as the new levy would be assessed upon profits, we do not think it would raise problems similar to those which gave rise to the derating of industrial properties.

## Chapter 12

### CONCLUSIONS, INCLUDING COMMENT ON THE BOARD OF INLAND REVENUE'S VIEWS OF 1912 ON THE FEASIBILITY OF A LOCAL INCOME TAX

THERE can be no doubt that the Swedish system of communal income tax is an effective method of raising revenue for local authorities. In Chapters 8 and 9 we considered the differences between the Swedish and the United Kingdom tax systems, and the effect they would have on the possibility of introducing a local income tax in the United Kingdom. While there is a close resemblance in the methods of defining income and a degree of similarity in the procedure for determining appeals, there is a basic difference in the administrative approach to assessment and collection in the two countries. So far as this difference can be condensed into a few words, it is that Swedish tax is on a personal basis, whereas in the United Kingdom the tax is keyed to the source of income. Apart from surtax, which follows the Swedish model, the British method is to tax the income when it first comes into existence, without paying much attention, at the point of assessment, to the persons who ultimately enjoy it. The house, the farm, the business are each the subject of charge to tax. In Sweden it is the ultimate recipient of the income who is taxed. The profits of a company distributed as dividends are taxed twice, and this double taxation, illogical though it seems to us, undoubtedly facilitates the working of a communal tax based on personal incomes.

Again in regard to employments, there is a vital distinction. The Swedish employee makes his contact with the tax administration after he has earned his income and suffered preliminary tax on it. He submits his return, his liability is assessed, and the amount of tax is adjusted.

His British counterpart makes his agreement with the Inland Revenue at the beginning of the tax year when he gets an agreed coding. After that the process for most employees is automatic, and they do not make returns of their earnings nor do they have another settlement with the Inland Revenue at the end of the year. This is perhaps to oversimplify the situation, but it does serve to focus the problem of the introduction of a local income tax into the United

Kingdom. Could the administration be redesigned so that a location could be given to all income at the point of assessment? If so a local tax could be assessed and collected at the same time as the national tax. It may be felt that the difficulties are too great and that there would be too much resistance to the fundamental changes which would be necessary.

There is an alternative approach. A local income tax administration could be set up which would employ the same basic information as the national system and yet work independently towards a separate assessment and payment. There would have to be machinery for putting the relevant information from national returns at the disposal of local authorities, and it would probably be necessary to set up a national body charged with the duty of apportioning the profits of industry and commerce. The administrative difficulties are formidable, but this seems to us more promising than an attempt to copy the Swedish system, and to leave scope for more flexibility in administration. In Sweden, the joint national and communal tax administration is divided into two sections on a functional basis, each dealing with both taxes. The first section has the responsibility for determining the amount of income. The remaining stages—assessment, allowances, calculation of duty, and collection—are dealt with by the second section in separate offices, sometimes in separate buildings. Without in any way minimising the difficulties, there seems to be more feasibility in a scheme of local income tax which would rely on an *ad hoc* organisation within each local authority charged with the responsibility for assessing and collecting local income tax. The chief difficulties are again concerned with employments. Remembering the 40 per cent incidence of movements, it is difficult to see how a PAYE system with rates variable according to the commune of residence could be worked without thrusting an impossible burden on the employers.

This leads up to the two conditions which the Board of Inland Revenue regarded as essential in 1912 when they submitted a memorandum on the feasibility of a local income tax to the Departmental Committee on Local Taxation, 1912-14 (Chairman, Sir John Kempe, KCB).

The Board's Memorandum is given in full in Appendix IV to this report. Paragraph 10 reads as follows:

Subject to certain conditions, however, though difficult, it would not be impossible to work the combination of a local income tax, at varying rates, with an Imperial income tax at a uniform rate, while maintaining the principle of collection at the source.

These conditions are:



## CONCLUSIONS

- (1) That the Local Income Tax should be assessed and collected in the first instance at a maximum rate, subject to the right of individual taxpayers to repayment of the difference between the tax at that rate and at the rate imposed in the area in which they reside.
- (2) That the proceeds of the tax be allocated by reference to the place of residence of the individuals who receive and enjoy the income.

The scheme which Viscount St. Aldwyn had advocated in evidence had little in common with the Swedish system. He had suggested the retention of rates and exchequer contributions to local services of a national character, for example police and education. He proposed to substitute for the "assigned revenues" which at that time were paid by the Exchequer to local authorities, a percentage of the national income tax collected from residents in the area of the authority. There was to be no additional taxation on any individual, merely the earmarking of part of the national tax for local revenues in lieu of the "assigned revenues." His suggestion for dealing with the proper attribution of the profits of a railway or a large bank had been as follows:

In each of those cases it must be remembered that a definite part of the undertaking is assessed to local rates somewhere. . . . I do not see why it should not be possible for the local authority which knows the local assessment to rates of that part of the undertaking which is within its borders, to send to the Inland Revenue a statement showing the amount of that assessment and the income rate in the £, which . . . would be leviable within the district of that local authority. The Inland Revenue then, having arrived at the whole profits of the undertaking, might divide the total amount of those profits among the several local authorities in proportion to the rateable value of that part of the undertaking which was within the limits of each authority; they would then on that part of the profits charge the income rate in the £ which the local authority was entitled to levy. . . . Finally, the bank or railway would lump the whole of those payments to the local authorities and charge them to their shareholders at an equal rate in the £, obtaining them from their shareholders just as they now obtain the income tax on the shareholders' dividends. . . .

There have been considerable changes since 1912. Graduation had been introduced in 1909, but there were only three rates: earned income up to £2,000, 9d.; up to £3,000, 1s. od.; and unearned income, 1s. 2d. Super tax began at £5,000. There was an exemption limit of £160 per annum which eliminated the wage earners and the lower ranges of salary earners. The total number of taxpayers was small compared with to-day and they were dealt with on personal returns, there being nothing comparable with the PAYE system.

The basic conditions have changed to such an extent that the qualified acceptance of the possibility of such a scheme, given by the Board of Inland Revenue in 1912, does no more than underline some of the difficulties which then attached to the system of deduction at the source. Those difficulties still exist, and are now augmented by the weightier difficulties arising out of PAYE and the wider spread of the activities of our large industrial organisations. For reasons given earlier in this report, the suggestions of Lord St. Aldwyn for splitting up the profits of a large undertaking solely on the basis of rateable property would not be equitable and might not prove practicable.

Points which particularly struck us in our study of the Swedish system were:

1. The continuity of rates of local income tax in times of prosperity and the confidence that no great difficulty need be anticipated in a trade recession.
2. The effect of the integration of the communal and national tax on the public attitude to local expenditure.
3. The value of a communal income tax in fostering local independence of the central government.

Another feature which needs no particular emphasis from us is that the size of the areas of rating authorities has a big influence on practicability. A scheme which might prove unworkable with 4,000 separate rating authorities, might be brought within the bounds of possibility if the number were reduced to, say, 400.

At the end of our enquiry we were left with some unresolved doubts in regard to the fundamental basis of the Swedish system:

1. Whether it is right that a salaried person should pay the whole of his local income tax to his district of residence and make no contribution to the cost of the local services in the area where he earns his income and enjoys the benefit of many local services during the greater part of the daylight hours.
2. Conversely, whether it is equitable that the individual trader should pay only where he makes his profit and contribute nothing to the local revenues of the area in which he resides.
3. Whether total income, with a complete disregard of the size of residence, should be the sole criterion of liability to contribute to local revenues.
4. Whether the repercussions of expanding the number of local

## CONCLUSIONS

ratepayers from the present figure around 14 millions to something in the region of 22 millions would not prove to be very formidable.

5. Whether there is any theoretical justification for allowing the local income tax to be deducted in all cases in computing income for purpose of the national tax.



# APPENDIX I

TABLE I

*The Swedish National Budget for Fiscal Year 1954*  
(1st July, 1953—30th June, 1954)

	Kr. millions	Per cent of total
Budgetary receipts:		
Direct taxes .. .. .	4,408	54.0
Indirect taxes and customs .. .. .	2,310	28.3
Automobile taxes .. .. .	611	7.5
Total taxes .. .. .	7,329	89.8
Government enterprises .. .. .	243	3.0
Other income .. .. .	586	7.2
Total receipts .. .. .	8,158	100.0
Budgetary expenditure:		
Social security, welfare and health ..	2,745	33.4
Education .. .. .	984	12.0
Communications .. .. .	741	9.1
Agriculture .. .. .	399	4.9
Interest on government debt .. .. .	357	4.4
Other expenditure .. .. .	844	10.4
Military services .. .. .	2,119	25.8
Total expenditure .. .. .	8,189	100.0

TABLE 2  
*An Analysis of the Aggregate Expenditure of Swedish Local Authorities, 1951*

	Cities (Städer)	Market towns (Köpingar)	Rural communes (Landskommuner) Municipalities (Municipalsamhället)	Counties (Landsing)	Total
	kr. 1,000	kr. 1,000	kr. 1,000	kr. 1,000	kr. 1,000
Police and fire brigade	151,098	7,450	40,235	—	198,783
Roads, parks and properties	438,045	29,498	10,878	—	478,421
Health services	263,338	1,436	13,416	493,545	771,735
Hygiene	215,656	19,980	5,852	—	241,488
Education	423,934	41,815	463,924	37,564	967,237
Welfare	291,121	17,894	181,596	21,679	512,290
Miscellaneous	98,739	9,741	279,304	3,702	391,486
	1,881,931	127,814	995,205	556,490	3,561,440
Harbours	77,440	203	213	—	77,856
Transport	68,747	—	—	—	68,747
Gas and electricity	393,707	13,457	4,074	—	411,238
	539,894	13,660	4,287	—	557,841

Administration .. .. .	79,007	6,535	1,707	11,222	98,471
Loan interest .. .. .	86,616	3,916	9,245	3,811	103,588
Loan repayment .. .. .	115,713	8,058	31,739	9,939	165,449
Share subscriptions .. .. .	84,548	1,064	1,269	—	86,881
	365,884	19,573	43,960	24,972	454,389
Total expenditure .. .. .	2,787,709	161,047	1,043,452	581,462	4,573,670
Included in above:					
Acquisition of property, and new construction:					
Tax-borne services .. .. .	372,114	37,851	216,573	63,524	690,062
Harbours .. .. .	27,065	60	98	—	27,223
Transport .. .. .	7,723	—	—	—	7,723
Gas and electricity .. .. .	84,881	3,987	885	—	89,753
	491,783	41,898	217,556	63,524	814,716



TABLE 3

*The Income of Swedish Local Authorities 1951 Analysed*

<i>Source of income</i>	<i>Cities (Städer)</i>	<i>Market towns (Köpingar)</i>	<i>Rural Communes (Landskommuner) Municipiums (Municipalsamhallen)</i>	<i>Counties (Landsting)</i>	<i>Total</i>
	<i>kr. 1,000</i>	<i>kr. 1,000</i>	<i>kr. 1,000</i>	<i>kr. 1,000</i>	<i>kr. 1,000</i>
Income from charges, rents, fees, interest, etc. .. .. .	470,908	25,005	185,845	98,619	780,377
Exchequer grants .. .. .	254,365	21,415	273,766	49,027	598,573
Local taxes .. .. .	1,051,735	74,772	458,874	395,223	1,980,604
	1,777,008	121,192	918,485	542,869	3,359,554
Income of public utilities:					
Harbours .. .. .	73,991	151	152	—	74,294
Transport .. .. .	49,855	—	—	—	49,855
Gas and electricity .. .. .	405,718	12,352	3,991	—	422,061
	529,564	12,503	4,143	—	546,210
Loans raised .. .. .	425,705	23,724	92,472	13,552	555,453
Total income .. .. .	2,732,277	157,419	1,015,100	556,421	4,461,217

TABLE 4

Swedish Local Authority Income from Exchequer Grants and Local Taxes 1951

Source of income	Cities		Market towns		Rural communes Municipiums		Counties		Total	
	kr. 1,000	%	kr. 1,000	%	kr. 1,000	%	kr. 1,000	%	kr. 1,000	%
Exchequer Grants										
Education .. ..	161,262	63	18,471	86	240,919	88	10,151	21	430,803	72
Health services .. ..	17,959	7	4	—	128	—	34,910	71	53,001	9
Welfare .. ..	10,897	4	340	2	4,563	2	1,489	3	17,289	3
Other purposes .. ..	47,416	19	2,544	12	24,069	9	2,477	5	76,506	13
Tax mitigation .. ..	—	—	56	—	4,087	1	—	—	4,143	—
Compensation for town customs .. ..	16,831	7	—	—	—	—	—	—	16,831	3
	254,365	100	21,415	100	273,766	100	49,027	100	598,573	100
	19.5%		22.3%		37.4%		11.0%		23.2%	
Local Taxes										
Communal income tax	1,031,638	98	73,495	98	451,875	98	395,223	100	1,952,231	98.5
Dog tax .. ..	1,471	2	286	2	3,610	2	—		6,043	1.5
Entertainment tax .. ..	16,852		981		3,375		—		21,208	
Artistes tax .. ..	275		8		12		—		295	
Other taxes .. ..	823		1		2		—		826	
	1,051,735	100	74,771	100	458,874	100	395,223	100	1,980,603	100
	80.5%		77.7%		62.6%		89.0%		76.8%	
Total income derived from taxation	1,306,100		96,186		732,640		44,250		2,579,176	
	100%		100%		100%		100%		100%	

TABLE 5  
*Summary of the Uppsala Budget for 1954 (p. 149)*

	Gross Expenditure kr.	Income		Net Expenditure kr.
		Charges, recoveries, etc., kr.	Exchequer grants, kr.	
General expenses	2,134,245	327,002	—	1,807,243
Police and courts	2,213,600	61,000	44,120	2,108,480
Planning and building	761,000	82,000	—	679,000
Defence	465,230	4,000	375,000	86,230
Fire brigade	1,029,700	33,600	—	996,100
Real estate and properties	1,636,852	1,102,529	—	534,323
Streets and parks	2,851,425	559,380	185,000	2,107,045
Health services	429,070	65,700	4,600	358,770
Public hygiene	3,770,300	1,752,604	—	2,017,696
Food hygiene	116,290	76,440	—	39,850
Education	10,945,746	493,293	4,683,254	5,769,199
Social welfare	8,999,484	1,943,000	279,160	6,777,324
Miscellaneous	290,692	178,900	50	111,742
Loan interest	647,413	—	—	647,413
Loan repayments	872,005	—	35,945	836,060
Unforeseen expenses	1,281,805	—	—	1,281,805
	*38,444,857	6,679,448	5,607,129	26,158,280
Tax Equalisation Fund contribu- tion	2,840,000	—	—	2,840,000
Special fund contributions	454,800	—	—	454,800
Deficiency from 1952	363,930	—	—	363,930
	42,103,587	6,679,448	5,607,129	29,817,010

\* Includes capital expenditure of kr.2,478,500



TABLE 6

## Assessment for Swedish State Income Tax for 1953 in Kr. Millions

	Individuals	Swedish companies	Economic associations	Other associations	All taxpayers
Estimated income from agricultural real estate	2,095.6	148.4	0.2	1.86	2,262.8
Estimated income from other real estate ..	303.8	44.2	15.3	4.0	367.3
Estimated income from trades, professions, etc.	2,047.7	2,227.3	73.7	6.0	4,354.7
Estimated income from employments, etc.	22,090.9	—	—	—	22,090.9
Estimated income from capital .. ..	605.1	30.1	1.5	26.6	663.3
Deduction of deficit on source of income	— 164.8	— 15.2	— 1.4	— 1.1	— 182.5
Total net income .. .. .	26,978.3	2,434.8	89.3	54.1	29,556.5
Deductions other than deficit on source of income .. .. .	3,186.2	306.5	12.9	8.4	3,514.0
Assessed income .. .. .	23,782.8	2,128.3	76.4	45.7	26,033.2
Taxable income .. .. .	17,097.8	2,128.3	76.4	45.7	19,348.2
Tax assessed .. .. .	2,751.2	834.7	24.4	6.9	3,617.2

## Assessment for Swedish State Property Tax for 1953 in Kr. Millions

	Individuals	Swedish companies	Economic associations	Other associations	All taxpayers
Taxable property .. .. .	27,702.6	11.5	9.7	1,237.9	28,961.7
Tax assessed .. .. .	174.3	0.2	0.0	1.8	176.3

TABLE 7  
*Numbers of Incomes in Sweden in Ranges of Income*  
*(Adapated from "Sveriges Officiella Statistik")*

<i>Range of income</i>	<i>Sterling equivalent at official exchange rate of kr. 14.5 to £</i>	<i>Sterling equivalent at kr. 16.0 to £</i>	<i>Number of incomes (000s omitted)</i>	<i>Percentage of total numbers</i>
Below kr. 1,200	83	75	175	4.69
1,200— 1,500	83— 104	75— 94	112	3.00
1,500— 2,000	104— 138	94— 125	207	5.54
2,000— 2,500	138— 172	125— 156	200	5.35
2,500— 3,000	172— 207	156— 188	179	4.79
3,000— 3,500	207— 242	188— 219	169	4.52
3,500— 4,000	242— 276	219— 250	155	4.15
4,000— 4,500	276— 311	250— 282	152	4.07
4,500— 5,000	311— 345	282— 313	147	3.94
5,000— 6,000	345— 414	313— 375	301	8.06
6,000— 7,000	414— 483	375— 438	322	8.62
7,000— 8,000	483— 552	438— 500	330	8.84
8,000— 10,000	552— 690	500— 625	584	15.64
10,000— 12,000	690— 828	625— 750	320	8.57
12,000— 15,000	828—1,034	750— 938	188	5.03
15,000— 20,000	1,034—1,372	938—1,250	108	2.89
20,000— 30,000	1,372—2,069	1,250—1,875	60	1.61
30,000— 50,000	2,069—3,448	1,875—3,125	19	.51
50,000—100,000	3,448—6,897	3,125—6,250	6	.16
over 100,000	over 6,897	over 6,250	1	.02
			3,735	100.00

TABLE 8

*Comparison of Numbers of Incomes by Ranges of Income before Tax 1951-52  
(in Sweden and United Kingdom)*

Range of total income	United Kingdom		Sweden	
	Number of incomes (000s omitted)	Percentage of number of incomes to the total	Number of incomes (000s omitted)	Percentage of total number in ranges £135 upwards
135— 150	450	2.22	97	3.05
150— 250	3,555	17.56	542	17.05
250— 500	10,250	50.62	1,252	39.41
500— 750	4,356	21.51	904	28.46
750— 1,000	819	4.04	210	6.61
1,000— 1,500	420	2.07	110	3.46
1,500— 2,000	145	.72	38	1.20
2,000— 3,000	125	.62	15	.47
3,000— 5,000	83	.41	6	.19
5,000—10,000	36	.18	3	.09
10,000—20,000	9	.04		
Over 20,000	2	.01		
	20,250	100.00	3,177	100.00
			Below £135 558	
			3,735	

Swedish incomes (converted at kr. 16 to £); numbers apportioned to correspond with the ranges in the British statistics.



TABLE 9  
*Comparison of Local and National Taxes at Various Income Levels  
in Sweden and the United Kingdom*

Salary per annum		Sweden		United Kingdom	
		£	Total	£	Total
£500	Local	47		12	
	National	25	72	32	44
£750	Local	79		23	
	National	54	133	93	116
£1,000	Local	110		35	
	National	86	196	178	213
£1,500	Local	174		46	
	National	192	366	353	399
£2,000	Local	238		58	
	National	340	578	528	586
£3,000	Local	365		70	
	National	692	1,057	1,088	1,158
£4,000	Local	493		81	
	National	1,103	1,596	1,713	1,794
£5,000	Local	721		93	
	National	1,534	2,155	2,388	2,481
£10,000	Local	1,258		104	
	National	4,020	5,278	6,313	6,417

### Notes

The above examples have been worked out on the basis of a married man with no children, no life assurance or pensions contributions, the income being entirely earned income.

*Sweden:* The allowances have been based on the assumption that the person is living in Cost-of-living Area IV. Local income tax has been calculated at a rate of 12.75 per cent and the national taxes at 110 per cent (1954-55) of the basic rate.

*United Kingdom:* For local tax purposes, the person is taken to be residing in a house of rateable value £10, £20, £30, £40, £50, £60, £70, £80, £90 for the respective incomes of £500, £750, £1,000, £1,500, £2,000, £3,000, £4,000, £5,000, £10,000. The rates are assumed to be 23s. 2d. per £1 (County Boroughs, England and Wales, 1954-55)

TABLE 10  
*United Kingdom: Estimated Effect on Householders and Non-Householders of a  
 Change from a Rating to a Local Income Tax System, at Different Income Levels*

Income level		Householders				Non-householders			
		With local rates		With local income tax		With local rates		With local income tax	
		£	Total	£	Total	£	Total	£	Total
500	Local	12		16				16	
	National	32	44	29	45	32	32	29	45
750	Local	23		27				27	
	National	93	116	86	113	93	93	86	113
1,000	Local	35		38				38	
	National	178	213	165	203	178	178	165	203
1,500	Local	46		61				61	
	National	353	399	332	393	353	353	332	393
2,000	Local	58		83				83	
	National	528	586	499	582	528	528	499	582
3,000	Local	70		128				128	
	National	1,088	1,158	1,014	1,142	1,088	1,088	1,014	1,142
4,000	Local	81		173				173	
	National	1,713	1,794	1,605	1,778	1,713	1,713	1,605	1,778
5,000	Local	93		218				218	
	National	2,388	2,481	2,230	2,448	2,388	2,388	2,230	2,448
10,000	Local	104		443				443	
	National	6,313	6,417	5,948	6,391	6,313	6,313	5,948	6,391



Income is taken as earned, and the figures relate to a married man with no children, no life assurance, and no pensions contributions. Householders are treated as occupying houses of rateable value of £10, £20, £30, £40, £50, £60, £70, £80 and £90 on the respective incomes of £500, £750, etc. The rates are assumed to be 23s. 2d. in the £ (average rate for county boroughs, England and Wales, 1954-55).

Local income tax has been calculated at 4.5 per cent of total income after deducting £150 personal allowance, thus:

Income .. .. .	£1,000
Personal allowance .. .. .	150
	<hr/>
	850
Local income tax at 4.5% .. .. .	38

In computing local income tax, no distinction is made between earned and unearned income. In the columns headed "With local income tax", the local tax as set out is deducted from income in calculating the national tax to accord with the Swedish pattern.

## APPENDIX II

### *Example of the Calculation of the Tax Mitigation Grant to Swedish Local Authorities*

#### 1. Local authority

Number of inhabitants	.. .. .	8,000
Total taxable income of area	kr. 9,600,000 or 96,000 skattekroner	
Average income per inhabitant	.. .. .	kr. 1,200
Total net expenses	.. .. .	kr. 1,728,000
Communal income tax required	.. .. .	kr. 18 per skattekrona
Yield of tax at kr. 18 on 96,000 skattekrona		kr. 1,728,000
Average expenditure per inhabitant	.. .. .	kr. 216

#### 2. Sweden

National average income per inhabitant	.. .. .	kr. 1,600
Shortfall in local authority income per inhabitant	.. .. .	kr. 400
Percentage of shortfall in local authority income	.. .. .	25
National average rate of communal income tax, taken at	.. .. .	kr. 11 per skattekrona
National average expenditure per inhabitant	.. .. .	kr. 176

#### 3. Calculation of grant

$$\begin{aligned}
 \text{Rate of Grant} &= \left( \frac{\text{local authority rate of tax required} - \text{national average rate of tax}}{\text{local authority income per inhabitant}} \right) \times \text{shortfall in} \\
 &= (18 - 11) \times 25 \\
 &= \text{kr. 1.75 per skattekrona} \\
 \text{Amount of grant} &= 96,000 \text{ skattekrona} \times 1.75 \\
 &= \text{kr. 168,000}
 \end{aligned}$$

#### 4. Tax levied by local authority

$$\begin{aligned}
 \text{Rate required after receipt of grant} &= \text{kr. 11} + 75\% \text{ of kr. } (18 - 11) \\
 &= \text{kr. 16.25 per skattekrona}
 \end{aligned}$$

#### 5. Statement of account

Net expenses of local authority	.. .. .	kr. 1,728,000
Less tax mitigation grant	.. .. .	168,000
		<hr/>
		kr. 1,560,000
		<hr/>
Tax yield = 96,000 skattekrona × 16.25	.. .. .	kr. 1,560,000
		<hr/>

## APPENDIX III

### *The Practice of the Inter-Communal Assessment Board*

This Appendix sets out the answers given to a number of questions relating to the Board's practice regarding apportionment of business income.

#### *(a) Apportionment of Income between Head Office Share, Manufacturing Profit and Sales Profit*

Under the provisions of Section 58 of the Communal Tax Law, 5 per cent of the income chargeable to communal tax will normally be allocated to the commune where the head office of the business is situated. In the case of a business which both manufactures goods and sells them through its own sales organisation, the balance of income is, in accordance with current practice, usually allocated as to two-thirds to manufacturing profit and as to one-third to sales profit. The manufacturing profit is allocated, where necessary, in proportion to output, or on any other basis which may be deemed reasonable, and the sales profit by reference to the turnover figures. Apportionment by reference to so-called special accounting in respect of various branch offices is not, as a rule, accepted.

In certain cases, however, the head office share is estimated at 10 per cent. The head office share of an enterprise which carries on a trading undertaking only, is accordingly generally computed at the higher percentage if the head office looks after the forwarding of goods purchased. The increase is justified by the fact that some part of the profit should be attributed to that part of the activity of the head office which is concerned with the purchase of goods and which, in the hands of the manufacturing company, is represented by manufacturing profit. Moreover, the head office share is usually computed at 10 per cent if the head office's responsibilities are unusually extensive, e.g., if extensive construction and research work is carried on in the commune of the head office, or if, as in the case of our great export industries, the head office attends to world-wide business. Finally, the head office share is usually increased to 10 per cent in any cases where, while the head office attends to the sales business, this requires a relatively small staff. It has been considered in such cases that the head office commune would be unduly favoured if it were allocated 5 per cent as head office share and one-third of the outstanding income as sales profit. The head office commune is credited with, instead, a smaller sales profit owing to the head office share being raised to 10 per cent: the balance of the income liable to communal tax being allocated to the manufacturing communes. The latter procedure is usually applied, moreover, where the manufacture involves goods of a fairly similar nature which are sold in large quantities. This applies, for example, in the case of mining



# THE FINANCE OF LOCAL GOVERNMENT IN SWEDEN

undertakings; similarly the sales profit of iron works and timber undertakings is often not calculated in accordance with the main rule, but the head office share is instead increased to 10 per cent.

## (b) *Distribution of Income where the Sales Comprise both Goods Manufactured and Goods Purchased*

The technical process of apportionment of profit in such a case is shown in the following example.

Basis: Business income liable to communal tax, kr. 50,000. Head office in Commune A. Total sales kr. 900,000 of which kr. 500,000 relates to goods manufactured, and kr. 400,000 to goods purchased. Sales in Commune A kr. 700,000, in Commune B kr. 200,000. Manufacture to be apportioned as to 60 per cent to Commune B and 40 per cent to Commune C.

The distribution should be computed in the following manner:

When the head office share (5 per cent  $\times$  kr. 50,000 = kr. 2,500) has been deducted, it is first determined what part of the outstanding amount consists of manufacturing profit. Then the part of the outstanding balance of kr. 47,500 which corresponds to manufacturing and sales profit on goods manufactured is computed. Since part of the goods have been both manufactured and sold, the turnover on these, in accordance with the normal scheduled two-thirds manufacturing profit and one-third sales profit, should be assigned a "factor" of 3 (2+1), resulting in  $3 \times$  kr. 500,000, while the turnover in respect of the goods purchased is assigned the factor 1, and is thus included at the actual amount, kr. 400,000. The manufacturing and sales profit on goods manufactured can therefore be computed as:

$$\frac{3 \times 500,000}{3 \times 500,000 + 400,000} \times 47,500 = \text{kr. } 37,500$$

Of the latter figure,  $\frac{2}{3} \times$  kr. 37,500 = kr. 25,000 comprises the manufacturing profit, of which 60 per cent (kr. 15,000) is allotted to commune B and 40 per cent (kr. 10,000) to commune C.

The sales profit on goods manufactured, kr. 12,500 (kr. 37,500 - 25,000), and on goods purchased, kr. 10,000 (kr. 47,500 - 37,500), total kr. 22,500, is apportioned as to  $700 \div 900 \times 22,500 =$  kr. 27,500 to commune A, and as to  $200 \div 900 \times 22,500 =$  kr. 5,000 to commune B.

The assessments will therefore be:

		kr.
Commune A	Head office share	2,500
	Sales profit	17,500
		<u>20,000</u>
Commune B	Sales profit	5,000
	Manufacturing profit	15,000
		<u>20,000</u>
Commune C	Manufacturing profit	<u>10,000</u>

### APPENDIX III

#### (c) *The Question of a Permanent Establishment for Sales*

The actual circumstances in a case which has been the subject of enquiry by the Commission were roughly as follows:

An undertaking which sells certain imported machines, rents premises in town B, in which the machines are demonstrated. From an office in the same premises a number of agents are directed. These solicit orders for the machines. The orders are confirmed from the head office in town A, and the goods are delivered to the customers from a free port warehouse in town C. In which towns does the undertaking carry on business from a permanent establishment?

In this case the sale is not regarded as having taken place in town B, as no cash transaction took place there, and as the staff at the office were not authorised to negotiate business. Neither has a sale been made in town C, inasmuch as the dispatch of goods alone without direct contact with the customer is not regarded as involving a sale. The whole of the income of the undertaking has therefore been assessed to communal tax in town A.

If sales profit is to be distributed in proportion to the turnover at various establishments, the amount of the sales in respect of business transacted at each establishment will correspond to the quoted turnover of that establishment. The place of dispatch of the goods is of no importance in this connection.

## APPENDIX IV

### Memorandum Submitted in 1912 by the Board of Inland Revenue to the Departmental Committee on Local Taxation

*Extract from the Appendices Attached to the Report of the  
Departmental Committee on Local Taxation, 1912-14  
(Chairman, Sir John Kempe K.C.B.), Cmd. 7315-6, 1914.*

1. The Departmental Committee on Imperial and Local Taxation ask to be favoured with our observations on evidence given before them by Lord St. Aldwyn with regard to the proposed introduction of a local income tax into the financial system of the country.

2. In November, 1899, we furnished at the request of the Royal Commission on Local Taxation a memorandum dealing (*inter alia*) with the practicability of levying for local purposes a tax on income derived from non-rateable property (Cd. 201, 1900, p. 205), and we supplemented that memorandum by a paper (p. 217) in which Sir Henry Primrose referred to considerations lying beyond the sphere of the mere practicability of such a tax.

3. The proposal of Lord St. Aldwyn has, however, a wider scope, and the question of its practicability raises different considerations.

On the other hand, the tax now proposed would not be confined to income from non-rateable property, and consequently it would escape the particular difficulties which, as we pointed out to the Royal Commission, are inherent in the isolation, for separate assessment, of income which might rightly be regarded as arising from non-rateable property.

On the other hand, the suggestion now made involves difficulties which did not arise in connection with the former proposal. The tax now suggested aims at being a true local income tax, which would be allocated to county councils and county boroughs by reference to the place of origin of the income, or to the place of residence of the person entitled to it. It is proposed to discontinue the assignment to local authorities of certain revenue which at present they receive from the Exchequer, derived from excise licences, beer and spirit duties, the estate duty grant, and the agricultural rates grant; and to empower those authorities to raise sums more than sufficient to make up the deficiency, by imposing a local income tax at rates not to exceed a maximum rate fixed by law, the tax to be assessed and collected by the Inland Revenue.

4. In support of the practicability of the proposal, it is said that Prussia has succeeded in combining a local income tax with the income tax which it levies for national purposes.



With regard to the Prussian precedent, it must be noted, *however*, that the national tax is not levied, like our income tax, at the source of the income. The Prussian system lends itself much more readily than ours to the allocation of income to subordinate areas, and to the imposition of a further tax at such rate or rates as may be desired in view of the requirements of the local authorities acting for those areas.

5. Notwithstanding the greater flexibility of an income tax of the Prussian type, we assume that for national purposes our Imperial income tax will continue to be levied as at present at the source. We think that there can be no question of the superiority of that system of assessment as a means of preventing evasion. And apart from the question of evasion, we may point out that under that system payment of tax is secured on a large amount of income which, although it accrues as annual profits, does not reach the pockets of individuals in that shape. In his evidence before the Select Committee on the Income Tax which reported in 1906 (No. 565), Sir Henry Primrose estimated the amount of this non-personal income at £50,000,000. At the present rate of duty the tax on this sum would amount to nearly £3,000,000, and the whole of it would be lost if our present system of assessment at the source were abandoned in favour of a tax assessed on the returns of the individuals who finally receive and enjoy the income. Moreover, there would be a further considerable loss in respect of income arising here, but received by persons resident abroad.

6. We think that a local income tax based on individual returns would be largely evaded. It is true that for the super-tax we have to rely on returns of this nature, but whatever measure of success may have attended the taxation in this manner of such conspicuous incomes as those exceeding £5,000, we do not consider that the results afford any reliable or even approximate indication of those attainable if the same method were applied to all incomes exceeding £160.

If it were possible to obtain any considerable portion of the local "income rate" by deduction at the source, the loss by evasion would be diminished. There are, however, as we shall show, great difficulties in the way of charging income tax at the source unless the duty be imposed at a uniform rate.

7. In his evidence (Questions 7590 and 7591) Lord St. Aldwyn made suggestions for examination by your Committee for the utilisation of payment at the source in respect of certain large classes of profits.

He proposed that business profits should be regarded for the purposes of the assessment and allocation of the local income tax as attributable to the various local areas in proportion to the rateable value of any premises occupied for the purposes of the undertaking in each area. We do not think that the principle of such an allocation is capable of being defended. The instance taken of a British railway does not afford a fair example of the practical working of such a scheme. A railway is rated by reference to the earning capacity of the line in the several local areas through which it passes. The problem is

a very complicated one and has led to endless litigation, but a solution of some sort has been found. It might not be altogether unreasonable to allocate the "income rate" of a British railway on a similar basis, though even here, in dealing with a personal tax, it would be contrary to such precedents as there are to ignore entirely the places of residence of the persons who receive the income.

But outside the limited class of the concerns which are rated by reference to profits, it could not be expected that the rateable value of the premises occupied would afford even a tolerable basis for the allocation of the income rate. Supposing that the railway were abroad, and belonged to an English company with an office in the City, or supposing that such a company owned a foreign mine or a foreign tramway, it would not be reasonable on that account to assign the whole of the "income rate" on those profits to the City. The place of residence of the shareholders and debenture holders would clearly have a better claim, and must be allowed at least to participate in the produce of the tax.

Apart from the question of principle, there is a further objection. Under the suggestion made, not only shareholders, but also creditors having a charge on the profits of a business carried on by any company or person, or entitled to any interest or annual payment out of such profits, would be required to submit to a deduction of income tax based on a calculation, the correctness of which they would be unable to check, for the rate to be deducted would depend on the varying rates imposed—possibly in many areas—and on the proportion of the profits attributed to each area. The system of assessment at the source, with its chain of attendant deduction, is only tolerable when the amount of deductions claimed can be readily checked, and if necessary challenged, by the persons who are called on to submit to them.

A further difficulty would arise. Some of the persons who participate in the income would be exempt, and would be entitled to claim a repayment of duty, but it would not be possible to allocate the repayment to the area which had received credit for the payment. If the ordinary income tax abatements, as well as the exemption for incomes not exceeding £160, were to be applied to the local income rate, the problem of obtaining payment at the source would become almost fantastically insoluble.

8. Another proposal for payment at the source suggested for the consideration of the Committee, related to income from the securities of British, Indian, Colonial, and Foreign Governments paid through bankers and financial houses. Under the plan proposed, incomes of this nature would be allocated to the area in which the person receiving the income resides. Therefore, save in the exceptional cases of persons having more than one residence, the mixed rate difficulty would not arise. But would not an intolerable burden be laid on the paying agents? If the tax is to be deducted as proposed on the payment of the interest, it would be necessary that the various local authorities should fix their rates of charge some time before the beginning of each year, in order that the paying agents might receive sufficient notice of what was expected



of them. They would then have to ascertain the place of residence of every individual to whom they made any payment, deduct the appropriate rate of tax, and when they paid it to us, give us sufficient information to enable us to credit each local area with its proper proportion.

Moreover, it must be remembered that the persons who receive the interest would frequently not be the persons entitled to the beneficial enjoyment of it; these securities are largely held by trustees, and the "income rate" deducted should be allocated to the place of residence of the beneficiaries.

We do not think the suggestion practicable, and we are sure that bankers would view it with consternation.

9. We considered these two particular suggestions at some length because they illustrate so well the difficulty of obtaining payment of income tax at the source unless it be levied at one uniform rate. Income often passes through several hands in its passage from its source to the people who have the beneficial enjoyment of it. As long as you are content to charge it at one fixed rate you can assess it at the source, and duly distribute its burden by successive deductions. If you desire to impose varied rates you must resort to other methods.

The imposition of separate rates on earned income was only possible for the reason that, in the words of the Select Committee of 1906, "this class of income is almost invariably directly assessed and collected." It is enjoyed by the persons in whose hands it arises. The committee had to consider the whole framework of the income tax, and whilst for the reason stated they recommended the introduction of a differential rate for earned income as a part of the ordinary income tax, they recognised that, for the purposes of the super-tax, it was necessary to resort to different methods and a separate assessment.

10. Subject to certain conditions, however, though difficult, it would not be impossible to work the combination of a local income tax, at varying rates, with an Imperial income tax at a uniform rate, while maintaining the principle of collection at the source.

These conditions are:

(1) That the local income tax should be assessed and collected in the first instance at a maximum rate, subject to the right of individual taxpayers to repayment of the difference between the tax at that rate and at the rate imposed in the area in which they reside.

(2) That the proceeds of the tax be allocated by reference to the place of residence of the individuals who receive and enjoy the income.

11. The scheme of the tax would be generally as follows:

(1) The local would be an addition to the Imperial tax, and would be collected as part of, and under the same conditions as, that tax at the highest rate imposed by any local authority, that rate not to exceed a maximum fixed by law.

(2) Whenever local authorities imposed income tax at less than this



highest rate, persons residing within the area under these authorities would, on making a claim to the Commissioners of Inland Revenue, be repaid the difference between the rate imposed and the highest rate.

(3) At a fixed date every year, the Commissioners of Inland Revenue would ascertain the difference between the total amount of income tax received by reason of the addition of local income tax at the highest rate, and (a) the amount of the refunds made on account of the difference between this rate and lower rates imposed by local authorities, plus (b) the estimated amount of the cost of collection. The balance would be available for allocation to local authorities proportionately to the contribution received from persons residing within the jurisdictions of those authorities.

(4) The contribution received from persons residing within the jurisdiction of a local authority would be calculated on the basis of returns of income made for the purpose by all such persons who are liable to income tax. In all cases where complete returns are now prepared in connection with claims for exemption, abatement, or differentiation, or for the payment of super-tax, no further return need be furnished for the purpose of the local income tax.

12. The disadvantages of this scheme are:

(1) The vast addition to the work of the Repayment Branch of the Inland Revenue Department. The cost of this, however, would be very small compared to what would be the loss from evasion if local income tax were collected as well as allocated on the basis of individual returns.

(2) The considerable sums which might be paid by taxpayers in the first instance in excess of the amounts ultimately due from them; and the trouble to which they would be put in obtaining repayment of the excess.

These, of course, are the disadvantages necessarily incidental to assessment at the source, and the existing income tax is open to objection on similar grounds. The question as to how far it is justifiable or desirable to go in collecting tax in excess of the ultimate net liability, in order that the State may enjoy the increased efficiency and equality of a tax assessed at the source, is one of degree. If the total amount to be raised by the local income tax is limited, or nearly limited, to the amount of the present Government contributions proposed to be withdrawn, the objections may not be considered as necessarily fatal to the scheme.

13. It must not be forgotten that the existing income tax extends over the whole of the United Kingdom. The scheme of taxation we have indicated contemplates the imposition and collection of duty in the first instance at a uniform total rate, and unless the local income tax covers the same area as the Imperial tax, the rate would not be uniform and the difficulty of obtaining payment at the source would be so greatly enhanced that the adoption of this scheme would probably be considered undesirable.

#### APPENDIX IV

14. If the objections to the above scheme for obtaining payment at the source are considered too serious, we think that the only alternative would be to obtain payment of any local income tax which may be imposed by the method of assessment based on the returns of individual taxpayers. This method, besides being, as already pointed out, greatly inferior in efficiency, would also involve a far larger expenditure in collection.

MATTHEW NATHAN

E. E. NOTT BOWER

18th October, 1912



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The main published sources from which the material in this report has been drawn are given below. No attempt is made to make the list comprehensive. The sources to the table given in Chapter IV, page 42, are quoted for each country under "Statistical Sources," together with other useful statistical publications. Periodicals and proceedings of societies are also mentioned. With the exception of Canada and the U.S.A., which are well documented, little published material on local finances is available in English on overseas countries, and a great deal of the information in the report was derived from unpublished materials and by direct correspondence with experts in the countries concerned. Very few references are therefore given under some countries.

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